SECURITIES VIOLATIONS IN 140 CHARACTERS OR LESS: SOCIAL MEDIA AND ITS GROWING IMPACT ON THE SECURITIES INDUSTRY

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I. INTRODUCTION

Over the last decade, the prevalence of social media across the globe has grown exponentially.[1] In a world where one billion people are currently connected to Facebook[2] and 400 million tweets[3] are being sent each day,[4] the effect of social media on society has become increasingly obvious. Companies and organizations have also availed themselves of the advantages of social media in order to reach out to a more extensive consumer base.[5] However, as technol-

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[1] *See Global Digital Communication: Texting, Social Networking Popular Worldwide*, PEW RESEARCH CTR. (Dec. 20, 2011), http://www.pewglobal.org/2011/12/20/global-digital-communication-texting-social-networking-popular-worldwide (stating that more than half of the people in the United States and Israel utilize social networking sites, while in three other countries, four out of ten people use these sites). According to the Securities and Exchange Commission, " '[s]ocial media' is an umbrella term that encompasses various activities that integrate technology, social interaction and content creation . . . including, but not limited to, blogs, microblogs, wikis, photos and video sharing, podcasts, social networking, and virtual worlds." *Investor Adviser Use of Social Media*, U.S. SEC. AND EXCH. COMM'N 1 (Jan. 4, 2012), http://www.sec.gov/about/offices/ocie/riskalert-socialmedia.pdf.

[2] *Facebook Key Facts*, FACEBOOK, http://newsroom.fb.com/content/default.aspx?NewsAreaId=22 (last visited Oct. 20, 2012).

[3] A "tweet" is a post limited to 140 characters or less that allows a user to share with others what they are currently doing at the moment. *Twitter*, TECHTERMS, http://www.techterms.com/definition/twitter (last visited Oct. 20, 2012).

[4] Dan Farber, *Twitter Hits 400 Million Tweets Per Day, Mostly Mobile* (June 6, 2012, 3:24 PM), http://news.cnet.com/8301-1023_3-57448388-93/twitter-hits-400-million-tweets-per-day-mostly-mobile/.

[5] *Regulatory Notice 10-06: Social Media Websites*, FINRA (Jan., 2010),

ogy progresses, the law must evolve accordingly. This has been particularly important for regulators of the securities industry, given the complexity and breadth of financial markets.[6]

The securities industry is primarily governed by the Securities Act of 1933 ("Securities Act")[7] and the Securities Exchange Act of 1934 ("Securities Exchange Act").[8] These federal acts were enacted to control credit in the market, prohibit market manipulation, and regulate the sale and offerings of securities by promoting full disclosure in order to protect the public from insider trading.[9] Additionally, the Financial Industry Regulatory Authority ("FINRA")[10] was established as a Self-Regulatory Organization ("SRO") to act as a supplemental regulatory entity.[11] FINRA's overarching mission is to regulate all facets of securities law, ranging from "registering and educating industry participants to examining securities firms; writing rules; enforcing those rules and the federal securities laws; informing and educating the investing public; providing trade reporting and other industry utilities; and administering the largest dispute resolution forum for investors and registered firms."[12] Therefore, the Securities and Exchange Commission ("SEC") and FINRA have the task of recognizing social media's effect on securities regulation and adapting accordingly.

Commonly referred to as the "information network," Twitter allows its users to broadcast information throughout the network in the form of a "tweet," which is limited to "140 characters [or less] in

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http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p120779.pdf.

[6] Strategic Plan Fiscal Years 2010-2015, U.S. SEC. AND EXCH. COMM'N 3 (June 7, 2010), http://www.sec.gov/about/secstratplan1015f.pdf.

[7] 15 U.S.C. 77a (1980).

[8] 15 U.S.C. 78a (2006).

[9] Philip A. Loomis, Jr., *The Securities Exchange Act of 1934 and the Investment Advisers Act of 1940*, 28 GEO. WASH. L. REV. 214, 217 (1959-1960).

[10] "FINRA was created in 2007 through the consolidation of the National Association of Securities Dealers (NASD) and the member regulation, enforcement, and arbitration functions of the New York Stock Exchange (NYSE)." Angela A. Hung et al., *Investor and Industry Perspectives on Investment Advisers and Broker-Dealers* 7, n.3 (2008), *available at* www.sec.gov/news/press/2008/2008-1_randiabdreport.pdf. Until the consolidation process of the FINRA rules is complete and approved, the FINRA rulebook contains both NASD rules and Incorporated NYSE Rules. *FINRA Rules*, FINRA, http://www.finra.org/Industry/Regulation/FINRARules (last visited Oct. 20, 2012).

[11] Tanja Boskovic et al., *Comparing European and U.S. Securities Regulations: MiFID versus Corresponding U.S. Regulations* 4 (World Bank, Working Paper No. 184, 2010).

[12] *About the Financial Industry Regulatory Authority*, FINRA, http://www.finra.org/AboutFINRA/ (last visited Oct. 20, 2012).

length."[13] The site hosts a forum of users ranging from the average person to celebrities and from businesses to news sources.[14] The variety of users which Twitter boasts creates a dangerous combination for the type of information that is disseminated and the speed at which it travels. Within seconds, a corporation has the ability to "tweet" a new product or press release which will inevitably reach millions of people. The site's growing popularity in the financial industry has the SEC and FINRA concerned with the content of those tweets.[15]

The antiquated regulations of the SEC are being tested nearly seventy years later with the Internet utilization of over thirty percent of the world's population.[16] The securities industry will have to adapt as the line between securities violations and the dissemination of information becomes increasingly unclear.[17] Furthermore, this type of powerful communication, combined with the allure of anonymity, has become particularly enticing to criminals.[18] It allows fraudsters to mass communicate with the public at low costs through easy-to-create accounts, in which their identity may never be discovered.[19]

This Comment demonstrates the drastic effects, both positive and negative, that social media has on securities regulation. Given the evolving laws, as well as the ever-growing power of social media, this Comment suggests, to both investment advisers and potential investors, to err on the side of caution when approaching these types of

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[13] *About*, TWITTER, https://twitter.com/about (last visited Oct. 20, 2012).

[14] *Help*, TWITTER, http://support.twitter.com/groups/31-twitter-basics/topics/104-welcome-to-twitter-support/articles/215585-twitter-101-how-should-i-get-started-using-twitter (last visited Oct. 20, 2012).

[15] *See Quarterly Disciplinary Review*, FINRA 2 (July 2011), http://www.finra.org/web/groups/industry/@ip/@enf/@da/documents/disciplinaryactions/p123818.pdf (summarizing a disciplinary action in early 2011, in which FINRA sanctioned a California broker because she had sent numerous posts containing "misrepresentative and unbalanced" investment advice through Twitter).

[16] *See Internet Users in the World: Distribution by World Regions—2011*, INTERNET WORLD STATS (Mar. 31, 2011), http://www.internetworldstats.com/stats.htm (showing 2,095,006,0005 as being the latest figure for the total of Internet users).

[17] *See Regulatory Notice 10-06*, *supra* note 5, at 2 ("The goal of this *Notice* is to ensure that—as the use of social media sites increases over time—investors are protected from false or misleading claims and representations, and firms are able to effectively and appropriately supervise their associated persons' participation in these sites.").

[18] *Investor Alert: Social Media and Investing—Avoiding Fraud*, U.S. SEC. & EXCH. COMM'N (Jan. 2012), http://www.sec.gov/investor/alerts/socialmediaandfraud.pdf.

[19] *Id.*

communications. Section II discusses the laws governing the securities industry and how they have evolved with the emergence of social media. Sections III and IV outlines how investment companies are currently dealing with this phenomenon, as well as highlights violations of securities laws through the use of social networks. Section V discusses why potential investors should be cognizant of social media-based investments, and lastly, section VI contemplates the future of securities regulation and social media's place in the securities industry.

II. EVOLUTION OF SECURITIES REGULATIONS

In October 1929, the Dow Jones Industrial Average ("DJIA") fell thirty percent in less than one week, foreshadowing the financial devastation that would lie ahead during the Great Depression.[20] It became clear "[t]here was a consensus that for the economy to recover, the public's faith in the capital markets needed to be restored."[21] The Senate Committee on Banking and Currency sought a solution through its extensive hearings regarding "stock market practices, which ultimately led to the enactment of the Securities Exchange Act."[22] The Committee's report described a variety of abuses that contributed to the Great Depression, including "extensive manipulation of prices on the exchanges by pools, options, and particularly the participation in such pool operations by issuers and their management and short-swing trading by officers and directors in the stock of their own companies, often on the basis of inside information."[23]

The Securities Act was the "[f]irst federal text to regulate securities," which, among other things, governed the "offering of securities" and demanded full disclosure by companies to all potential buyers.[24] The SEC was established shortly thereafter upon passage of the Securities Exchange Act.[25] Considering its responsibility, the

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[20] *See* Boskovic et al., *supra* note 11, at 5.

[21] *The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, U.S. SEC. & EXCH. COMM'N, http://www.sec.gov/about/whatwedo.shtml#create (last modified Mar. 12, 2012) [hereinafter *About SEC*].

[22] Loomis, Jr., *supra* note 9, at 217.

[23] *Id.*

[24] Boskovic et al., *supra* note 11, at 5.

[25] *Id.* The Securities Exchange Act also provided further regulations for the exchange of existing securities, and criminalized insider trading. *Id.*

SEC would have to be powerful enough to be able to regulate and supervise countless firms, brokers, and investment advisers.[26] Currently, the SEC has five commissioners, "organized into five [d]ivisions and eighteen [o]ffices" in Washington, D.C., and staff members in eleven of the most notable cities of the United States.[27] According to the SEC, several common violations may yield an SEC investigation, including: "misrepresentation or omission of important information about securities; manipulating the market prices of securities; stealing customers' funds or securities; violating broker-dealers' responsibility to treat customers fairly; insider trading (violating a trust relationship by trading on material, non-public information about a security); and selling unregistered securities."[28]

In addition to federal law, SROs such as FINRA also work to supervise securities transactions, and "control the [organization] and business conduct of brokers and dealers."[29] Some of these organizations' responsibilities overlap, as the SEC supervises the United States Exchanges, while both the SEC and FINRA regulate the secondary market.[30] FINRA is a non-profit organization with the sole mission "to protect America's investors by making sure the securities industry operates fairly and honestly."[31] In doing so, FINRA supervises 4,900 securities firms and nearly 660,000 brokers and subjects those firms to thorough examination.[32]

Federal securities regulations also strictly govern the conduct of investment advisers.[33] An investment adviser can be an individual or a firm that provides guidance regarding securities transactions,[34]

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[26] *About SEC*, *supra* note 21.

[27] *About SEC*, *supra* note 21; *see also Securities and Exchange Commission*, U.S. SEC. & EXCH. COMM'N, http://www.sec.gov/images/secorg.pdf (last visited Oct. 20, 2012) (outlining the organization of the Securities and Exchange Commission).

[28] *About SEC*, *supra* note 21.

[29] Boskovic et al., *supra* note 11, at 9. The Securities Exchange Act defines a "broker" as "any person engaged in the business of effecting transactions in securities for the account of others." 15 U.S.C. 78a § 3(A)(4) (2006). A "dealer" is defined as "any person engaged in the business of buying and selling securities for such person's own account through a broker or otherwise." 15 U.S.C. 78a § 3(A)(5) (2006).

[30] Boskovic et al., *supra* note 11, at 6. However, under the Securities Exchange Act Section 19(d)(2), any disciplinary actions by FINRA are subject to appeal to the SEC. *Id.*

[31] *Brochure*, FINRA, http://www.finra.org/web/groups/corporate/@corp/@about/documents/corporate/p118667.pdf (last visited Oct. 20, 2012).

[32] *Id*. at 3.

[33] *The Laws that Govern the Securities Industry*, U.S. SEC. & EXCH. COMM'N, http://www.sec.gov/about/laws.shtml#invcoact1940 (last modified Aug. 30, 2012).

[34] *Investment Advisers: What You Need to Know Before Choosing One*, U.S. SEC. & EXCH.

and is subject to strict registration requirements.[35] These requirements are an absolute necessity, as their advice and analyses facilitate transactions that would affect securities markets, the national banking system, and the national economy.[36] Investment advisers are primarily governed by the Investment Advisers Act of 1940, which emphasizes three primary obligations: (1) increased fiduciary duties, (2) duties to report and retain records, and (3) miscellaneous requirements, which include registration requirements.[37] Therefore, because these heightened standards apply to investment advisers, it is more difficult for firms to regulate all aspects of investment advisers' behavior on social media platforms.

A. FINRA Regulatory Guidance

In order to properly regulate the securities industry, the SEC and FINRA must reconcile the out-of-date rules with the evolving technology. Over the past few years, the regulatory organizations have made great strides in this regard. As the Internet became more widespread in the 1990s, FINRA released several clarifications regarding communications and interactive web sites.[38]

First, FINRA addressed the issue of registered representatives and chat rooms by declaring this interaction to be subject to the same requirements as a presentation in person "before a group of investors."[39] The guidelines for these types of communications with the public are enumerated in National Association of Securities Dealers ("NASD") Rule 2210.[40] Communications under this rule include advertisements,[41] sales literature,[42] correspondence,[43] institutional sales

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COMM'N, http://www.sec.gov/investor/pubs/invadvisers.htm (last modified Aug. 20, 2010).

[35] *See* Boskovic et al., *supra* note 11, at 17 (explaining that brokers and dealers must, among other things, be registered with the SEC, "become a member of an SRO," comply with state requirements, and be subject to an inspection to ensure the broker-dealers are complying with the governing provisions).

[36] 15 U.S.C. § 80b-1 (2006).

[37] Hung et al., *supra* note 10, at 12.

[38] *Regulatory Notice 10-06*, *supra* note 5, at 1.

[39] *RCA—March 1999—Ask the Analyst—Electronic Communications*, FINRA, http://www.finra.org/Industry/Regulation/Guidance/RCA/p015326 (last visited Oct. 20, 2012).

[40] *NASD 2210: Communications With the Public*, FINRA, http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=3617 (last visited Oct. 20, 2012) [hereinafter NASD 2210].

[41] *Id.* at (a)(1).

Any material, other than an independently prepared reprint and institu-

material,[44] and public appearances.[45] These types of communications must also satisfy the content standards which apply to "[a]ll [c]ommunications with the [p]ublic."[46] The rule expressly requires that all communications should be founded on fair dealing and good faith, and must "provide a sound basis for evaluating the facts in regard to any particular security or type of security, industry, or service."[47] Furthermore, "[n]o member may publish, circulate or distribute any public communication that the member knows or has reason to know contains any untrue statement of a material fact or is otherwise false or misleading."[48]

The rule regarding communications is also inherently intertwined with aspects of supervision and approval.[49] According to NASD Rule 3010, governing supervision, each member must have a system in place to supervise registered representatives' or registered principals' activities, such as the approval of advertisements, sales li-

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> tional sales material, that is published, or used in any electronic or other public media, including any Web site, newspaper, magazine or other periodical, radio, television, telephone or tape recording, videotape display, signs or billboards, motion pictures, or telephone directories (other than routine listings).

Id.

[42] *Id.* at (a)(2).

> Any written or electronic communication, other than an advertisement, independently prepared reprint, institutional sales material and correspondence, that is generally distributed or made generally available to customers or the public, including circulars, research reports, performance reports or summaries, form letters, telemarketing scripts, seminar texts, reprints (that are not independently prepared reprints) or excerpts of any other advertisement, sales literature or published article, and press releases concerning a member's products or services.

Id.

[43] NASD 2210, *supra* note 39, at (a)(3).

[44] *Id.* at (a)(4).

[45] *Id.* at (a)(5). "Participation in a seminar, forum (*including an interactive electronic forum*), radio or television interview, or other public appearance or public speaking activity." *Id.* (emphasis added).

[46] *Id.* at (d)(1).

[47] *Id.* at (d)(1)(A).

[48] NASD 2210, *supra* note 39, at (d)(1)(B).

[49] *See NASD 3010: Supervision*, FINRA, http://finra.complinet.com/en/display/display_main.html?rbid=2403&element_id=3717 (last visited Oct. 20, 2012) ("Each member shall establish and maintain a system to supervise the activities of each registered representative, registered principal, and other associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with applicable NASD Rules.").

terature, and independently prepared reprints.[50] Subsequent to the principal approval of a registered principal, certain advertisements, depending on the content, must be filed with the FINRA's Advertising Regulation Department.[51]

These rules would become the foundation for FINRA's stance towards social media web sites.[52] In September 2009, FINRA assembled a Social Networking Task Force to investigate how social media may be used in the securities industry without compromising investor safety.[53] FINRA issues notices regularly to discuss and interpret current rules, proposed rules for which it is soliciting comment, and rules of governmental agencies, such as the SEC.[54] In January 2010, FINRA issued its first attempt to provide guidance regarding social media issues and their current regulations in "Notice 10-06."[55] The notice provided preliminary guidance on problematic issues such as advertising, compliance, recordkeeping, and supervision of social networking web sites, blogs, and other communications with the public.[56] Specifically, NASD Rule 2210, governing communications to the public, was the focus of "Notice 10-06."[57]

Within this notice, FINRA attempted to make an important distinction between static and non-static (interactive) content on social media sites.[58] "[S]tatic content remains posted until it is changed

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[50] *Id.*

[51] *Filing Communications for FINRA Review*, FINRA 2, http://www.finra.org/web/groups/industry/@ip/@edu/documents/education/p017549.pdf (last updated Dec. 31, 2011). Communications that contain content regarding "mutual funds, variable annuities, variable life insurance products and exchange trade funds" must be filed with FINRA. *Id*.

[52] *See Regulatory Notice 10-06*, *supra* note 5, at 1-2 ("FINRA has provided guidance concerning particular applications of the communications rules to interactive Web sites in the past.").

[53] *Id.*

[54] *Types of FINRA Notices*, FINRA, http://www.finra.org/Industry/Regulation/Notices/p085286 (last visited Oct. 20, 2012).

[55] *Regulatory Notice 10-06*, *supra* note 5 ("Americans are increasingly using social media Web sites . . . for business and personal communications. Firms have asked FINRA staff how the FINRA rules governing communications with the public apply to social media sites . . . . This *Notice* provides guidance to firms regarding these issues.").

[56] *See id.* (listing the Notice 10-06's key topics).

[57] *See id.* (describing the ways that FINRA has provided past guidance on the applicability of communications rules to the Internet, but stating that "[n]evertheless, FINRA staff has continued to receive numerous inquiries from firms and others concerning how the FINRA rules governing communications with the pubic apply to the use of social media sites by firms and their required representatives").

[58] *Id.* at 5.

by the firm or individual who established the account on the site . . . [and is generally] accessible to all visitors to the site."[59] Such content would require approval by a registered principal of the firm before it may be posted.[60] To the contrary, non-static, interactive content, such as chat rooms and interactive blogs, are deemed public appearances and do not require principal approval, but rather, are subject to other supervisory requirements by the firm.[61] However, "[s]ocial networking sites typically contain both static and interactive content."[62] It is also possible for interactive content to become static, which makes the regulation of social networks much more difficult.[63] Notice 10-06 attempted to clear up any ambiguities, and stated that firms must approve all static content such as profiles, backgrounds, or any wall information.[64] Furthermore, interactive posts through Twitter and Facebook should be monitored post-use to ensure the content does not violate any other FINRA or SEC rules.[65]

Additionally, Notice 10-06 suggests that firms adopt internal policies and procedures to ensure proper use of social networking platforms.[66] This recommendation is important for several reasons. First, firms must continue to retain any records in accordance with the Securities Exchange Act and NASD Rule 3110 that concern

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[59] *Id.* Websites, bulletin boards, and blogs are examples of "[s]tatic (non-interactive) content," also characterized as advertisements. *Guide to the Web for Registered Representatives*, FINRA, http://www.finra.org/industry/issues/advertising/p006118 (last visited Oct. 20, 2012).

[60] *Id.* FINRA defines a "Registered Principal" as:

> Persons associated with a member who are actively engaged in the management of the member's investment banking or securities business, including supervision, solicitation, conduct of business, or the training of persons associated with a member for any of these functions are designated as principals . . . [which] include sole proprietors, officers, partners, managers of offices of supervisory jurisdiction, and directors of corporations.

FINRA Registration and Examination Requirements, FINRA, http://www.finra.org/industry/compliance/registration/qualificationsexams/registeredreps/p011051 (last updated Nov. 9, 2011).

[61] *Regulatory Notice 10-06*, *supra* note 5, at 4-5.

[62] *Id.* at 5.

[63] *See id.* ("As with other Web-based communications such as banner advertisements, a registered principal of the firm must approve all static content on a page of a social networking site established by the firm or a registered representative before it is posted.").

[64] *Id.*

[65] *Id.*

[66] *Regulatory Notice 10-06*, *supra* note 5, at 7.

"business as such."[67] Second, there is also a concern that posts made by firms or employees, may be reposted somewhere else by a third party.[68] Typically, a firm would not be held responsible for such content unless the firm 1) was involved in preparing the content, or 2) "explicitly or implicitly endorsed or approved the content."[69] Therefore, firms should be extremely prudent in the types of posts they allow their employees to disseminate on their behalf, as it may result in their liability.

Lastly, Notice 10-06 confirmed that a firm's recommendation of a security through a social media site must satisfy NASD Rule 2310 governing suitability.[70] This becomes particularly important because of the great extent in which social media sites allow users to reach one another.[71] According to Notice 10-06, one may determine whether a post is a recommendation based on the "facts and circumstances of the communication."[72] The "facts and circumstances" standard surrounding communications has become an important but very vague phrase, ultimately causing firms to wait and see which communications actually constitute crossing the line.[73]

Following Notice 10-06, FINRA issued Notice 11-39 in August 2011 to address unanswered questions, as well as to clarify the more narrow issues surrounding the new technologies.[74] First, record-keeping pursuant to Securities Exchange Act Rule 17(a)(4) concerns many firms because they are obligated to retain any records

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[67] *Id.* at 3.

[68] *Id.* at 7.

[69] *Id.* The first requirement is also referred to as the "entanglement theory" by the SEC, which occurs when a "firm or its personnel is entangled with the preparation of the third-party post." *Id.* at 8. The second requirement is also referred to as the "adoption theory" by the SEC, which occurs when a "firm or its personnel has adopted its content." *Regulatory Notice 10-06*, *supra* note 5, at 7.

[70] *Id.* at 3. Under NASD Rule 2310, a broker-dealer may only make recommendations to a customer if that recommendation is appropriate for *that* investor, considering their investor's portfolio, finances, and goals. Hung et al., *supra* note 10, at 9.

[71] *See Regulatory Notice 10-06*, *supra* note 5, at 3 ("Various media sites include functions that make their content widely available or that limit access to one or more individuals.").

[72] *Id.*

[73] *See Investment Adviser Use of Social Media*, *supra* note 1, at 3 n.10 (providing a "non-exhaustive list of factors that an investment adviser may want to consider when evaluating the effectiveness of its compliance program").

[74] *Regulatory Notice 11-39: Social Media Websites and the Use of Personal Devices for Business Communications*, FINRA (Aug. 2011), http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p124186.pdf.

regarding "business as such."[75] Therefore, if a client is obtained through a social media platform and discussions begin surrounding possible business transactions, these communications must be retained.[76] In order to comply with the retention rule, Notice 11-39 suggests that firms have policies and procedures in place, which allow employees to properly distinguish between personal and business social networking accounts.[77] Furthermore, FINRA makes clear that it does not matter if the communication is made on a personal device or a firm's computer because it must be retained as long as it relates to "business as such."[78] In effect, the more freedom that a firm gives its employees to perform their responsibilities from various devices and locations, the more difficult it will be to monitor and retain such communications.[79]

As previously stated, firms must supervise the content that is disseminated by employees in order to comply with the advertising rule, as well as to avoid liability from third party posts.[80] Considering the difficulty of this task, firms were uncertain as to how they should supervise properly.[81] Notice 11-39 addressed the concern of supervision with regard to social media compliance by recommending several measures a firm should take.[82] First, to ensure compliance, firms must train and educate their members about the policies.[83] In addition, firms should take note of members who have had prior difficulties with compliance.[84] This imposes an obligation on the firm to follow up on these "red-flags."[85] Failure to do so may result in a violation of the duty to supervise.[86]

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[75] *Id.* at 3.

[76] *Id.*

[77] *Id.*

[78] *Id.* at 7.

[79] *Regulatory Notice 10-06*, *supra* note 5, at 3 ("A firm's policies and procedures must include training and education of its associated persons regarding the differences between business and non-business communications and the measures required to ensure that any business communication made by associate persons is retained, retrievable and supervised.").

[80] *See Regulatory Notice 10-06*, *supra* note 5, at 5, 7 (describing the ways that a firm may become responsible for posts made by third parties).

[81] *See Regulatory Notice 11-39*, *supra* note 74, at 1 (noting the uncertainty experienced by firms).

[82] *Id.* at 5.

[83] *Id.*

[84] *Id.*

[85] *Id.*

[86] *Regulatory Notice 11-39*, *supra* note 74, at 5 (discussing the measures a firm should

Notice 11-39 also addressed third-party posts, third-party links and websites, and co-branding.[87] After Notice 10-06, firms wanted to clarify specifically the type of conduct which may be characterized as involvement in the preparation of the content or explicit or implicit endorsement or approval of the content.[88] The latest notice also cautions firms that associated persons may answer questions using social media platforms, but the communication must fall within the boundaries of the firm's policies.[89] One way to ensure that substantive answers are not conveyed to the third party is by allowing firms to provide pre-approved statements to direct third parties on firm-approved content or official means of communication, such as a business e-mail system.[90] Not only would this limit third party liability, but it also would ensure that business-related communications are maintained within the associate's business accounts, thereby allowing them to be properly retained by the firm. Also, under NASD Rule 2210, "a firm that co-brands any part of a third-party site, such as by placing the firm's logo prominently on the site, is responsible for the content of the entire site."[91] The firm will be considered to have adopted the content of a third party post if the firm explicitly or implicitly endorses the post.[92] Therefore, under certain facts and circumstances, a firm will be liable for all of a site's content if it adopts or becomes entangled with the third-party content, or has reason to know that the site has content that is false or misleading.[93] In order to prevent adoption, firms should have policies in place that block or delete inappropriate content.[94]

B. Regulation of Investment Advisers

Given the tremendous responsibility and power of investment advisers, federal laws demand the more meticulous supervision of investment advisers.[95] For instance, firms are required to keep the

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take to properly supervise its employees).

87 *Id.* at 6.

88 *See id.* (asking when a firm will not be held responsible for third-party content).

89 *Id.*

90 *Id.*

91 *Regulatory Notice 11-39*, *supra* note 74, at 6.

92 *Id.*

93 *Id.*

94 *Id.*

95 The "Findings" section within the Investment Advisers Act describes the power that

records of investment advisers for at least five years.[96] The primary communications that must be retained include records of client interactions, as well as the termination of investment advisers' fiduciary duties.[97] Also, it includes all transactions of the advisory firm, all employee transactions, copies of the firm's advertisements and client communications, and any record evincing performance-based advertisements.[98] These records are retained in accordance with the federal law because the Securities Exchange Act, the Investment Advisers Act, and the Investment Company Act of 1940 authorize the SEC to conduct examinations of the SEC-registered firms, including their employees.[99] The purpose of the examinations is to ensure that these firms are complying with federal securities laws, making the proper disclosures to investors, and maintaining policies in place to promote internal compliance with the law.[100]

Investment advisers are utilizing social media sites to communicate with current clients, solicit potential clients, as well as to promote their services.[101] Social networks give advisers a platform to reach millions of people within moments—a power susceptible to abuse.[102] Therefore, if a firm chooses to experiment with a social media program for their employees, each communication must be monitored and maintained in accordance with federal law.[103] A recent report in Massachusetts conducted by the Securities Division of the Office of the Secretary of the Commonwealth surveyed registered investment advisers to determine the scope of their use of social media, and their policies for record retention and supervision.[104] It is

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advisers have and how that may influence the global market. 15 U.S.C. 80b-1 (2006).

[96] Hung et al., *supra* note 10, at 13.

[97] *Id.*

[98] *Id.*

[99] *Examination Information for Broker-Dealers, Transfer Agents, Clearing Agencies, Investment Advisers, and Investment Companies*, U.S. SEC. & EXCH. COMM'N 1, http://www.sec.gov/about/offices/ocie/ocie_exambrochure.pdf (last visited Oct. 20, 2012).

[100] *Id.*

[101] *Investor Adviser Use of Social Media*, *supra* note 1.

[102] *See, e.g.*, *In re* Migliozzi II, Securities Act Release No. 9216, 2011 WL 2246317, at *3 (June 8, 2011) (allegedly violating section 5(c) of the Securities Act); In re Fields, Securities Act Release No. 9291, 2012 WL 19759, at *2 (Jan. 4, 2012) ("Fields made multiple fraudulent offers of fictitious bank guarantees and MTNs on social media website LinkedIn.").

[103] *Investment Adviser Use of Social Media*, *supra* note 1, at 2.

[104] *Report on Massachusetts Registered Investment Advisers' Use of Social* Media, SEC'Y OF THE COMMONWEALTH OF MASS., http://www.sec.state.ma.us/sct/sctmediasurvey/socialmedia.pdf (last visited Oct. 20, 2012) [hereinafter *Massachusetts Report*].

clear the "growing trend" has been to use these sites to solicit new investors, while continuing to foster existing relationships.[105] Of the 450 investment advisers surveyed, forty-four percent responded that they "used some form of social media."[106] The survey indicated that LinkedIn[107] is the most frequent social media network used, more than twice as often as firms' websites.[108]

LinkedIn is also known as the "professional network," which allows users to connect with friends and co-workers, then use those connections to further their company or career.[109] It currently boasts executives from all 2011 Fortune 500 companies as some of its members.[110] The company then allows users to create personal pages, which resemble a resume, or a company page, which represents the company as whole.[111] The distinction between company and personal pages becomes less distinct and more controversial when it comes to investment advisers.[112] For instance, consider an investment adviser who has listed his professional experience on his profile, as well as his company's website, in the standard template of the profile page. Should this be considered a personal page with a link simply describing the user's profession, or rather conduct indicative of soliciting new clients? It depends. If it is being used as a resume to be read by employers, then it may be considered personal communication.[113] However, if the profile also lists the firm's services, the communication would most likely be considered a business communication.[114]

Another feature of LinkedIn allows other users to connect with one another and write testimonies endorsing the skill and reputation of the user as a professional.[115] However, users are allowed to

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[105] *Id.*

[106] *Id.*

[107] *About Us*, LINKEDIN, http://press.linkedin.com/about (last visited Oct. 20, 2012).

[108] *See Massachusetts Report*, *supra* note 104 ("Most investment advisers using social media websites hosted by other parties used LinkedIn [forty-one percent], followed by Facebook [fourteen percent], and Twitter [eight percent].").

[109] *About Us*, *supra* note 107.

[110] *Id.*

[111] *Id.* ("More than [two] million companies have LinkedIn Company Pages.").

[112] *See Investment Adviser Use of Social Media*, *supra* note 1, at 5 ("A firm may consider whether to adopt policies and procedures to address an IAR or solicitor conducting firm business on personal (non-business) or third-party social media sites.").

[113] *Regulatory Notice 11-39*, *supra* note 74, at 4.

[114] *Id.*

[115] *Recommendations—Overview: How do Recommendations Work?*, LINKEDIN,

pick and choose which recommendations may appear on their page.[116] According to Rule 206(4)(1) of the Investment Advisers Act, SEC-registered investment advisers are forbidden from including advertisements that contain fraudulent, deceptive, or manipulative statements.[117] Although there are some exceptions, the rule is interpreted broadly to include testimonials of clients' experiences or endorsements, or past, specific recommendations made by the advisers "which were or would have been profitable."[118] Allowing advisers to select only the favorable recommendations to appear on their pages gives investors the false impression that the adviser has a high probability of success. Such a misleading practice would surely violate Rule 206(4)(1) of the Investment Adviser Act. The SEC has stated that even the use of the "Like" button[119] on Facebook by third parties may constitute an advertisement under Rule 206(4)(1), if the post is an "explicit or implicit statement of a client's . . . experience with [the] investment adviser."[120]

For example, "FINRA fined [a] registered representative $10,000" and issued a year-long suspension from working with any member firm because of several FINRA violations.[121] The representative maintained "two websites that included misrepresentations about her career" and did not request the requisite approval from her employer.[122] Furthermore, the representative maintained a Twitter account with over 1000 followers and sent out over thirty-two tweets regarding a security in which she and her family had an interest.[123] To prevent the misuse of social media seen in this case, each investment firm will have to evaluate how it will adapt to the changing climate.

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https://help.linkedin.com/app/answers/detail/a_id/90 (last visited Oct. 20, 2012).

[116] *Recommendations: Let Colleagues, Clients or Suppliers Speak to Your Record*, LINKEDIN, http://learn.linkedin.com/profiles/recommendations/ (last visited Oct. 20, 2012).

[117] 17 C.F.R. § 275.206(4)-1(a) (2006).

[118] 17 C.F.R. § 275.206(4)-1(a)(2) (2006).

[119] Facebook's "Like" feature allows users to "give positive feedback or to connect with things [they] care about . . . without leaving a comment." *Liking on Facebook*, FACEBOOK, http://www.facebook.com/help/like (last visited Oct. 20, 2012).

[120] *Investment Adviser Use of Social Media*, *supra* note 1, at 6.

[121] *Quarterly Disciplinary Review: July 2011*, FINRA 3 (July 2011), http://www.finra.org/web/groups/industry/@ip/@enf/@da/documents/disciplinaryactions/p123818.pdf.

[122] *Id.*

[123] *Id.*

III. HOW INVESTMENT FIRMS HAVE DEALT WITH SOCIAL MEDIA

The potentially harmful effects that social media may have on an investment firm are tremendous, but so are the potential benefits. Access to social media can give investment advisers and firms access to current and prospective clients instantly, for better or worse. It is this predicament that investment firms struggle with when trying to establish a suitable pilot program.[124] An investment adviser survey conducted by Socialware in 2011 reveals that eighty-four percent of the respondents indicated that they use social networks for business purposes, eighty percent have social media policies in place, but forty-two percent have no archiving process.[125] Developing such a program must be carefully crafted by a firm's marketing and legal/compliance department, and strictly adhered to by investment advisers.[126] Firms have dealt with this issue in a variety of ways, but it appears that most have erred on the side of caution.[127] Since the technology and regulations are still very new and many of the violations are determined by the facts and circumstances surrounding a communication, firms do not want to be the first to be made an example of.

A. Personal v. Business Use of Social Networking

Firms first dealt with compliance and use of employees' technology after the emergence of electronic mail and bulletin boards.[128]

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[124] *See* Andrew Osterland, *MSSB Advisers Get Green Light for Social Media*, INVESTMENT NEWS (June 25, 2012), http://www.investmentnews.com/article/20120625/FREE/120629953# ("While regulators have suggested that they would treat interactions over social-media networks as they do other forms of communications with customers and potential clients, the wirehouses have been wary of the potential risk to reputation that friending, tweeting and linking might pose for them.").

[125] *Executive Summary: Social Media Use by Financial Advisors*, SOCIALWARE (Sept. 2011) http://www.limra.com/pdfs/events/sm/11FinancialAdvSurvey.pdf.

[126] *See* Osterland, *supra* note 124 (explaining how Morgan Stanley Smith Barney ensured the social media pilot program was in full-compliance with governing regulations).

[127] *See Investment Adviser Use of Social Media*, *supra* note 1, at 3 n.10 ("Firms are encouraged to consider the factors described herein in assessing the effectiveness of their compliance program and implementing improvements that will best protect their clients. Firms are cautioned that these factors . . . are neither exhaustive nor will they constitute a safe harbor nor a 'checklist' for SEC examiners.").

[128] *See* FINRA's preliminary guidance regarding compliance and electronic communications. *Ask the Analyst—Electronic Communications*, *supra* note 39.

These firms are now faced with some of the same problems in regulating social media, such as differentiating between personal and business social networking accounts and the use of personal devices, which were then issues addressed in FINRA Regulatory Notice 11-39.[129] The use of personal and business social networking accounts raises much larger issues regarding supervision.[130] In order to comply with the SEC laws, there must be adequate supervision of the employees' communications (particularly investment advisers) and proper retention of such records concerning business matters.[131] Given the size and breadth of these types of companies, it would be nearly impossible to supervise and retain every post, tweet, or "Like" that an employee makes on a private or business social networking account, but the content is determinative.[132]

However, since investment advisers are typically held to a higher standard than other employees, it may be in the firm's best interest to focus on their accounts and activities.[133] To do so, firms have employed companies which have developed the technology to block words or actions that may raise red flags for non-compliance with the program's guidelines.[134] Actiance is an example of one of these companies which first emerged when compliance with e-mail and instant messaging became an issue.[135] According to Actiance, the company "can record . . . content regardless of what device or what location [they] posted it from," as well as "both an individual's personal profile and the [firm's] business page."[136] This may be done by logging on "through application programing interfaces provided by the social media website operators."[137] Another way this can be

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[129] *Regulatory Notice 11-39*, *supra* note 74, at 7.

[130] *See id.* ("The firm must be able to retain, retrieve and supervise business communications regardless of whether they are conducted from a device owned by the firm or by the associated person.").

[131] *Id.* at 2.

[132] *See Investment Adviser Use of Social Media*, *supra* note 1, at 6 ("RIAs that communicate through social media must retain records of those communications if they contain information that satisfies an investment adviser's recordkeeping obligations under the Advisers Act. In the staff's view the content of the communication is determinative.").

[133] *Id.* at 1-2.

[134] *See* David F. Carr, *Helping Financial Advisors With Social Media Compliance Hazards*, BRAIN YARD (May 2, 2011), http://www.informationweek.com/thebrainyard/news/social_networking_consumer/229402623 (discussing the ways in which to help firms comply with social media hazards).

[135] *Id.*

[136] *Id.*

[137] *Id.*

accomplished is by requiring users to "reach sites like Facebook by relaying through the . . . service so it can monitor and police their actions."[138]

B. Social Media Pilot Programs

Prominent firms, such as Morgan Stanley Smith Barney (hereinafter "Morgan Stanley") are experimenting with social media through "pilot programs."[139] Morgan Stanley was the "first major wealth manager to allow its brokers partial use of Twitter . . . [a]nd it is the latest wealth adviser to permit the use of LinkedIn."[140] The firm uses specialized programs "to capture and retain all communication on approved networking sites . . . [and] distribute research and content, such as status updates and tweets, but only those approved in advance by the firm."[141] The pilot program began with a small "test group" of 600 employees, but has now expanded to approximately 17,000 financial advisers who may "continue to draw from a prewritten library of Twitter messages and submit all LinkedIn postings for approval."[142] Lauren W. Boyman, Morgan Stanley's head of social media, acknowledged the risks and difficulties associated with regulating social network use, stating: "It's a lot harder to approve 140 characters than one might think it would be . . . . Pretty much every tweet has a link to a report or an article or a Web site, and all that has to get read and approved."[143]

Wedbush Securities is another leading investment firm that has authorized the use of Twitter, LinkedIn, and Facebook for its employees.[144] Contrary to other pilot programs, Wedbush is "encouraging its staff to join the on-going dialogue and not to rely solely on 'canned' statements, which will still be provided to supplement con-

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[138] *Id.*

[139] *See* Joseph A. Giannone, *Morgan Stanley OKs Broker Use of Social M*edia, REUTERS (May 25, 2011, 10:09 AM), http://www.reuters.com/article/2011/05/25/morganstanley-socialmedia-idUSN2510487920110525 (allowing its brokers "partial use of Twitter").

[140] *Id.*

[141] *Id.*

[142] William Alden, *Morgan Stanley to Expand Access to Social Media* (June 25, 2012, 12:16 PM), http://dealbook.nytimes.com/2012/06/25/morgan-stanley-to-expand-financial-advisers-access-to-social-media/.

[143] *Id*.

[144] Press Release, Wedbush Securities Gives Firm-Wide "Green Light" to Engage in Social Media, WEDBUSH (Jan. 10, 2012), http://www.socialware.com/about/news/wedbush-securities-gives-firm-wide-green-light-to-engage-in-social-media/ [hereinafter Wedbush].

versations with corporate information and activities."[145] Wedbush has employed Socialware to ensure compliance with securities laws, as well as to train and inform employees about effective social media usage.[146] A representative of Wedbush Securities indicated the program would allow investment advisers to utilize their "personalities" to connect with others.[147]

The SEC's cease-and-desist proceeding, *In re Fields*,[148] in January 2012 may have prompted the SEC's release of an Investor Alert[149] and National Examination Risk Alert.[150] The main goals of these alerts were to raise investor awareness of fraudulent schemes, aid those investment advisers engaged in social media to comply with usage and content standards, and implement proper compliance programs.[151]

The National Examination Risk Alert set out a list of non-exhaustive factors that investment advisers should consider when assessing whether a firm's compliance policies are effective.[152] The SEC suggests that a firm first determine the extent to which it would like its employees to utilize social media platforms.[153] A firm should

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[145] *Id*.

[146] *Id*.

[147] *Id*.

[148] Securities Act Release No. 9291, Exchange Act Release No. 66091, Investment Advisers Release No. 3348, Investment Company Release No. 29912, File No. 3-14684 (Jan. 4, 2012).

[149] *See Investor Alert*, *supra* note 18 ("The SEC's Office of Investor Education and Advocacy is issuing [an] Investor Alert to help investors be better aware of fraudulent investment schemes that may involve social media. U.S. retail investors are increasingly turning to social media, including Facebook, YouTube, Twitter, LinkedIn and other online networks for information about investing.").

[150] *See Investment Adviser Use of Social Media*, *supra* note 1. The following are the "Key Takeaways":

> Investment advisers that use or permit the use of social media by their representatives, solicitors and/or third parties should consider periodically evaluating the effectiveness of their compliance program as it relates to social media. Factors that might be considered include usage guidelines, content standards, sufficient monitoring, approval of content, training, etc. Particular attention should be paid to third party content (if permitted) and recordkeeping responsibilities.

Id.

[151] Ben Cole, *SEC Stress Importance of Social Media Guidelines and Compliance*, SEARCHCOMPLIANCE (Jan. 16, 2012), http://searchcompliance.techtarget.com/news/2240114006/SEC-stresses-importance-of-social-media-guidelines-and-compliance.

[152] *Investment Adviser Use of Social Media*, *supra* note 1, at 3-5.

[153] *Id.* at 3.

then analyze the potential risk to itself and its clients before placing the proper restrictions on the use of social media networks, whether it is a complete ban, or specific functionalities of a site.[154] The same limitations apply to the content of communications, such as whether investors should be limited to sharing information on investment services or be allowed the freedom to make investment recommendations.[155] Firms should also have a policy regarding how often they will monitor investment advisers' conduct.[156]

Also, keeping in mind the type of communication involved, firms should consider pre-approval or post-review of their communications.[157] Firms must be familiar with the social networking site being used to fully understand their exposure liability, and this includes the site's reputation, its privacy policy, "the ability to remove third-party posts," and whether anonymous posting is permitted.[158] An important measure firms should consider is the implementation of a training or certification program to ensure that investment advisers are aware of the power of social media and how it should be used in accordance with the firms' internal policies.[159] These factors are non-exhaustive and should not be considered a "safe harbor" or a "checklist" during SEC examinations.[160]

IV. NOTABLE VIOLATIONS

The adverse impact of social media on the securities industry is apparent. The Securities and Exchange Commission has discovered several schemes that have utilized social networks in order to create a profit.[161] According to the SEC, Michael Migliozzi II and Brian William Flato created a website called "BuyaBeerCompany.com" in an effort to raise three hundred million dollars for the purchase of Pabst Brewing Company.[162] The preliminary fundraising was done by soliciting individuals' contact information and pledge amounts, using their websites, as well as their Facebook and Twitter

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154 *Id.*
155 *Id.*
156 *Id.*
157 *Investment Adviser Use of Social Media*, *supra* note 1, at 4.
158 *Id.*
159 *Id.*
160 *Id.* at 3 n.10.
161 *Investor Alert*, *supra* note 18, at 3.
162 *Migliozzi II*, 2011 WL 2246317, at *1.

accounts.[163] Once the desired amount was reached, Migliozzi and Flato collected the pledge amounts from each individual.[164] In four months, the defendants collected over two hundred million dollars from over five million investors, and planned to incorporate their business, which would then distribute stock in the ownership, rather than a certificate of ownership.[165] In June 2011, Migliozzi and Flato were ordered to cease and desist ("the Order") by the Securities and Exchange Commission.[166]

Migliozzi and Flato's fundraising strategy is a common technique referred to as "crowdsourcing," which is "the use of social media and the Internet to organize a large group of individuals to achieve a common goal, [and] in this instance, to raise capital."[167] Their attempt to crowdsource was undoubtedly successful; however, in allegedly doing so, Migliozzi and Flato violated provisions of the Securities Act of 1933.[168] Subsequently, the Migliozzi and Flato consented to the issuance of the Order without either admitting or denying any of the claims alleged by the SEC.[169] In this scenario, the Securities Act of 1933 did exactly what it was enacted to do: regulate the offering of securities.

In June 2010, the SEC brought an action against Canadian residents Carol McKeown and Daniel F. Ryan alleging several violations of the Securities Act.[170] The two Canadians owned the website, "PennyStockChaser," which claimed to use its "team of research analysts, stock brokers, investment bankers, and traders [to] conduct[] thorough research on stocks and companies to recommend stock purchases to the investing public."[171] Using Facebook and Twitter, the site would distribute daily alerts to subscribers promoting certain stocks and, in return, were distributed shares of stock from the issuers.[172] For example, the defendants utilized the website to promote the stock of Converge Global, "a . . . corporation . . . in the business

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[163] *Id.* at *1-*2.

[164] *Id.* at *1.

[165] *Id.* at *2.

[166] *Id.* at *3.

[167] *Migliozzi II*, 2011 WL 2246317, at *1.

[168] *Id.* at *3.

[169] S*EC News Digest: Issue 2011-110*, U.S. SEC. & EXCH. COMM'N (June 8, 2011), http://www.sec.gov/news/digest/2011/dig060811.htm.

[170] Complaint at 1, SEC v. McKeown, No. 10-80748 (S.D. Fla. June 23, 2010).

[171] *Id.* at 4.

[172] *Id.*

of acquiring and developing properties."[173] The stock was first touted on May 11, 2009, when the website published: "[Converge]—Last @ .022—Up 16% on Friday—Ready to Move Higher . . . . [Converge] has the potential to jump 500%."[174] Subsequently, three more posts were added over a period of three weeks and the stock's price jumped from 1.9 cents per share to 2.2 cents per share, and a trading volume of 311,160 shares, to almost 4 cents per share and a trading volume of 16,098,530 shares.[175] A month and a half later, the defendants allegedly sold their 6.3 million shares for a profit of approximately $602,000.[176] McKeown and Ryan allegedly made similar transactions with six different companies, "realiz[ing] at least $2.4 million in net proceeds from their scalping scheme."[177]

The SEC filed its initial complaint alleging violations of Sections 17(A)(1), 17(A)(2), 17(A)(3) and 17(b) of the Securities Act and Section 10b-5 of the Securities Exchange Act.[178] A default judgment was entered against the defendants, ordering them to pay $3,719,543 in disgorgement fees.[179] It is clear that the use of social media in this instance allowed the defendants to reach a vast audience instantaneously. An advantage to using a social network such as Twitter is that it not only reaches the user's audience, but it allows posts to be "retweeted" by followers, which may then be posted and disseminated through that person's network as well.[180] Their social media access, combined with the failure to disclose material facts regarding the recommendations, allowed them to allegedly make profits that far exceeded the typical profits of a scalping scheme.[181]

Earlier this year, on January 4, 2012, the SEC initiated an order instituting administrative and cease-and-desist proceedings

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[173] *Id.* at 6.

[174] *Id.*

[175] Complaint, *supra* note 170, at 7.

[176] *Id.*

[177] *Id.* at 2. "Scalping is a trading style specializing in taking profits on small price changes, generally soon after a trade has been entered and has become profitable." *Scalping: Small Quick Profits Can Add Up*, INVESTOPEDIA (July 9, 2012), http://www.investopedia.com/articles/trading/05/scalping.asp#axzz1bcLJMsTx.

[178] Complaint, *supra* note 170, at 14-16.

[179] SEC v. McKeown, Litigation Release No. 21847, 2011 WL 457966, at *1 (Feb. 9, 2011).

[180] *See What is a Retweet?*, TWITTER, http://support.twitter.com/groups/31-twitter-basics/topics/109-tweets-messages/articles/77606-what-is-retweet-rt (last visited Oct. 20, 2012) (explaining how to Retweet).

[181] *McKeown*, 2011 WL 457966, at *1.

against Anthony Fields, a CPA, doing business as Anthony Fields & Associates and Platinum Securities Brokers.[182] In addition to alleging violations of offering fictitious securities on social media platforms, the SEC claims Fields used these websites "to offer to buy and sell fraudulent bank guarantees and medium term notes ("MTNs") in exchange for transaction-based compensation."[183] Fields registered his sole proprietorships with the SEC in which he was the "founder, president, chief compliance officer, and sole control person" of each entity.[184] However, Fields was "neither registered with the Commission as a broker-dealer nor licensed as an associated person of a registered broker-dealer."[185]

With neither of these qualifications, Fields allegedly made offers to "induce the purchase of fictitious securities," which, if proven, directly violates Sections 17(a)(1) and 17(a)(3) of the Securities Act and Sections 206(1) and 206(2) of the Advisers Act.[186] The following passage is an example of a post Fields had allegedly made on his personal LinkedIn page:

> Medium Term Notes, Cash Backed, Deutsche Bank, Credit Suisse, HSBC, JPMorgan Chase, BNP Paribas, UBS, RBS or Barclays, Ten (10) years and one (1) day. Fresh Cut 7.5% expected. USD 500 Billion (USD 500,000,000,000) with Rolls and Extensions. 30% or better plus 1% Commission Fees to be paid, to buy side and Sell side consultants 50/50. First Tranche 500 M USD. All interested parties can email me for particulars . . . .[187]

After seeing the posts on Fields' LinkedIn page, several interested investors contacted Fields.[188] Fields claimed that he was a funded investment adviser and broker dealer, even though he was unfunded and falsely represented to the SEC that he had $400 million in assets under management.[189] Among other things, Fields allegedly made material representations to clients and prospective clients by

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182 *Fields*, 2012 WL 19759, at *1.
183 *Id.*
184 *Id.*
185 *Id.* at *2.
186 *Id.* at *2, *4, *5.
187 *Fields*, 2012 WL 19759, at *2.
188 *Id.*
189 *Id.*

claiming his sole proprietorship, Anthony Fields & Associates, had $50 billion in U.S. Treasury securities, and its affiliate, Platinum, was a registered broker dealer and primary dealer licensed by the Federal Reserve Bank of New York to trade Treasury securities directly.[190]

These alleged violations of securities regulations are exactly the type of social media abuses that the SEC and FINRA fear will become more prevalent in the future. It is clear from the SEC alerts that prevention and awareness are important ways to deter fraudulent investments through social media platforms.

V. HOW DOES SOCIAL MEDIA AFFECT POTENTIAL INVESTORS?

In general, social media has become an easy and cost-efficient resource for potential investors to research stocks, broker-dealers and investment advisers, strategies, and other market trends.[191] Many inexperienced investors may be tempted by the false assurance of earning quick returns on investments, and therefore it is important to be wary of these practices.

The SEC issued the Investor Alert in January 2012, which outlined how and why social media platforms are commonly used for fraudulent practices, to facilitate the recognition of fraudulent investment offers by less experienced investors.[192] The SEC specifically mentions five tips which may aid an investor in identifying potentially fraudulent conduct.[193] First, it is imperative to "[b]e wary of unsolicited offers to invest," as the use of spam is a common tool for potential fraudsters.[194] Second, investment offers typically raise several "red flags," such as investments that promise to yield "INCREDIBLE GAINS" or "HUGE UPSIDE AND ALMOST NO RISK!"[195] These types of offers "are hallmarks of extreme risk or outright fraud," especially those that promise or guarantee returns on investments with little or no risk.[196] Third, "affinity fraud" is a type of offer that is made "based solely on the recommendation of a member of an organization or group to which [one] belong[s], especially if

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[190] *Id.* *3.

[191] *Investor Alert*, *supra* note 18, at 1.

[192] *Id.*

[193] *Id.* at 1-2.

[194] *Id.* at 1.

[195] *Id.* at 2.

[196] *Investor Alert*, *supra* note 18, at 2.

the pitch is made online."[197] This type of fraud may be especially deceiving because an offer which is reposted by a friend in a Facebook or LinkedIn group may appear to be more legitimate than it actually is. Another important tip is to be mindful of privacy settings, so personal information may only be accessed by friends and family.[198] Last, thorough research must be conducted before any investment is made, in order to ensure that the investment is viable.[199]

The SEC also cited the most common examples of fraudulent investment conduct, which included "[p]ump-and-dump" market manipulation, "high-yield investment programs," and "Internet-[b]ased [o]fferings."[200] Pump-and-dump schemes involve fraudsters who create small increases in stock price by reporting misleading statements, so when investors begin to buy the stock and the stock price rises, insiders will sell their shares.[201] High-yield investment programs and Internet-based offerings are typically unregistered investments and promise large returns on investments with little or no risk.[202] These fraudulent practices in combination with the unique elements of social media sites like Facebook and Twitter create a dangerous environment for potential investors.[203]

These guidelines minimize the number of fraudulent-offer victims and increase awareness to enable the public to recognize and report this type of conduct.[204]

VI. THE FUTURE OF SECURITIES REGULATIONS AND SOCIAL MEDIA

As the number of Facebook users surpasses one billion, it is evident that social media will remain a permanent fixture in society, and as its use increases, it will continue to infiltrate all aspects of our daily lives. Although firms initially may be tentative about embracing this technology, the ultimate decision to adopt a social media

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[197] *Id.* "Even if you do know the person making the investment offer, be sure to check out everything—no matter how trustworthy the person seems who brings the investment opportunity to your attention." *Id.*

[198] *Id.*

[199] *Id.*

[200] *Investor Alert*, *supra* note 18, at 3-4.

[201] *Id.* at 3.

[202] *Id.* at 3-4.

[203] *Id.* at 1.

[204] *Id.* at 4.

program will be inevitable.

According to Chris Brockius, Socialware CEO, 2012 was the year in which firms and investment advisers would be able to gain a competitive advantage by using social media.[205] Brockius specifically refers to the success of Mark Scribner, a Morgan Stanley adviser, who has fully embraced social media as a part of his profession.[206] Scribner reconnected with a business acquaintance after fifteen years through LinkedIn and within days received a large life insurance policy to manage, as well as a $2.6 million 401k account.[207] Early users, such as Scribner, have a decisive advantage over those who are hesitant to adopt such programs because they have already developed a method and strategy to access current and potential clients through these communications.

Organizations, such as the Securities Industry and Financial Markets Association ("SIFMA"), have made it a point to educate the securities industry about the importance of social media, as well as how to comply with the developing laws and regulations.[208] SIFMA is an organization whose sole mission is to promote the growth and success of the financial market.[209] Understanding the endless opportunities that social media holds for the securities industry, SIFMA has collaborated with social media companies such as Socialware, Smarsh, and HearsaySocial to sponsor seminars with important panelists representing FINRA, as well as officers from prominent investment firms.[210] Events like this allow for an interactive forum in which members of the securities industry can ask more specific questions to better understand how to use social media platforms in accordance with the governing laws and regulations.[211]

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[205] Chris Brockius, Socialware CEO, 2012 Social Media in Financial Services Predictions (Jan. 12, 2012), http://www1.socialware.com/2012-predictions-webinar.html.

[206] *Id.*

[207] Jennifer Hoyt Cummings, *For This Financial Adviser, Tweets are Good Business*, WALL STREET JOURNAL (Dec. 28, 2011, 8:35 AM), http://blogs.wsj.com/deals/2011/12/28/for-this-financial-adviser-tweets-are-good-business/.

[208] *SIFMA Mission*, SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, http://www.sifma.org/about/mission/ (last visited Oct. 20, 2012) ("SIFMA's mission is to develop policies and practices which strengthen financial markets and which encourage capital availability, job creation and economic growth while building trust and confidence in the financial industry.").

[209] *Id.*

[210] *Social Media Seminar Program*, SECURITIES INDUSTRY AND FINANCIAL MARKETS ASSOCIATION, http://www.sifma.org/events/2011/social-media-seminar/program (last visited Oct. 20, 2012).

[211] *Id*.

However, recent legislation may undercut the SEC's efforts in regulating Internet-based investments and crowdsourcing. In short, the JOBS Act has been enacted as a package of legislative acts that would allow small business and startups more leeway in raising capital, in an effort to promote the growth of small business, as well as job creation.[212] The JOBS Act was signed into law on April 5, 2012 and, among other things, modified Section 4 of the Securities Act to exempt issuers from certain requirements when offering and selling up to one million dollars in securities.[213] Although the Obama administration strongly supported this statute, the SEC, consumer advocate groups, and the North American Securities Administrators Association ("NASAA") opposed it.[214]

While the initial legislation was still pending, former SEC chief accountant Lynn E. Turner stated that the Act, among other things, would " 'destroy safeguards dating as far back as the laws that created the' SEC."[215] With regard to the crowdfunding legislation, SEC Chairman Mary L. Schapiro noted that the crowdfunding exemption "needs additional safeguards to protect investors from those who may seek to engage in fraudulent activities . . . [and without such] investor confidence in crowdfunding could be significantly undermined and would not achieve its goal of helping small business."[216] She stated that in order to better protect investors, the

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[212] *Jobs Act*, MAJORITY LEADER, http://majorityleader.gov/uploadedfiles/JOBSACTOnePager.pdf (last visited Oct. 20, 2012).

[213] *Jumpstart Our Business Startups Act: Frequently Asked Questions About Crowdfunding Intermediaries*, U.S. SEC. AND EXCH. COMM'N (May 7, 2012), https://www.sec.gov/divisions/marketreg/tmjobsact-crowdfundingintermediariesfaq.htm.

[214] Marlene Y. Satter, *JOBS Bill Under Fire by SEC, NASAA, Consumer Advocates* (Mar. 13, 2012), http://www.advisorone.com/2012/03/13/jobs-bill-under-fire-by-sec-nasaa-consumer-advocat.

[215] Thomas Waldron, *Former SEC Official Slams House JOBS Act: "It Won't Creat Jobs, but it will Simplify Fraud*, THINKPROGRESS (Mar. 15, 2012, 11:55 AM), http://thinkprogress.org/economy/2012/03/15/444951/jobs-act-simplify-fraud/?mobile=nc. Turner also stated at her testimony before the Senate Committee on Banking, Housing, and Urban Affairs, that the legislation, "reduces the level of transparency and amount of information investors will receive . . . removes critical investor protections put in place to protect against a repeat of scandals . . . [and] decreases the credibility of the information one will receive." *Spurring Job Growth Through Capital Formation While Protecting Investors, Part II Before the Senate Committee on Banking, Housing, and Urban Affairs* (2012) (Statement Lynn E. Turner, Former SEC Chief Accountant), *available at* http://banking.senate.gov/public/index.cfm?FuseAction=Files.View&FileStore_id=5aaabb66-36eb-4b1e-8195-3cbeda832814.

[216] Letter from Mary L. Schapiro, SEC Chairman, to Hon. Tim Johnson, Chairman of Committee on Banking, Housing, and Urban Affairs, and Hon. Richard C. Shelby, Ranking

Commission should have the authority to provide oversight of the intermediates that enable offerings to the public.[217] This type of regulation may prove to be difficult if offerings take the form of "tweets," for example, which are disseminated at such a rapid pace. Keeping in mind these potential issues, the SEC now has the duty to promulgate new rules, more specifically, to lift the prohibition of general advertising to allow crowdfunding.[218]

The recent developments regarding the JOBS Act will certainly add a different dimension to regulating securities and crowdsourcing. Nevertheless, within the last two to three years, FINRA and the SEC have made great strides in expanding the existing securities laws to govern the use of social media. However, this is just the beginning. As the use of this technology becomes more prevalent, more complex issues are sure to arise, especially in regard to multinational firms. Although the immediate future of social media is uncertain, this promising technology will undoubtedly contribute to the growth and success of the securities industry.

Member of Committee on Banking, Housing, and Urban Affairs (Mar. 13, 2012), *available at* http://ourfinancialsecurity.org/blogs/wp-content/ourfinancialsecurity.org/uploads/2012/03/Schapiro-to-Johnson-Letter-3-14-12.pdf.

[217] *Id.*

[218] *Information Regarding the Use of the Crowdfunding Exemption in the JOBS Act*, SEC. AND EXCH. COMM'N, http://sec.gov/spotlight/jobsact/crowdfundingexemption.htm (last modified Apr. 23, 2012).