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## CATCH-22.COM: Conflicting Social Media Regulatory Regimes and the Impact on Financial Institutions



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**B**roker-dealers and other financial advisory firms have recently found themselves caught between multiple overlapping and conflicting regulatory regimes when it comes to the use of social media by their employees and other associated persons. The cen-

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tral issue is whether companies have the right or the responsibility to monitor the “business-related” activities of their associated persons on social media sites.

On the one hand, the Financial Industry Regulatory Authority (FINRA) and the Securities and Exchange Commission (SEC) expect broker-dealers and registered investment advisers to take steps to monitor employees’ use of social media, retain records of such activity and ensure that employees do not harm investors through misleading or otherwise improper posts. On the other hand, both the National Labor Relations Board (NLRB)<sup>1</sup> and various state laws have placed significant limitations on employers’ ability to monitor or restrict employee social media usage.<sup>2</sup> These conflicting regulatory regimes place regulated firms in the untenable position of having to risk violating certain laws in order to comply with others.

<sup>1</sup> The NLRB’s rulings in some of these cases have been found invalid for a lack of properly-appointed quorum of NLRB members. See *Noel Canning v. NLRB*, 705 F.3d 490 (D.C. Cir. 2013), cert. granted, 133 S. Ct. 2861 (2013). The Supreme Court heard oral argument on Jan. 13, and a ruling should be issued in the coming months. Regardless of how the Supreme Court rules, however, the Senate’s confirmation last summer of a full slate of NLRB members has returned the NLRB to full and properly constituted status, and the new NLRB may simply re-issue and affirm any overturned decisions.

<sup>2</sup> Congress also is considering legislation similar to what many states have enacted. The Social Networking Online Protection Act (H.R. 537) had six Democratic co-sponsors and one Republican co-sponsor as of March 4. The lone Republican co-sponsor sits on the House Financial Services Committee.

## Financial Industry Regulations

FINRA requires broker-dealers to monitor for employee misuse of personal social media accounts for business purposes and can subject broker-dealers to periodic examinations to ensure compliance.<sup>3</sup> Specifically, “[f]irms must adopt policies and procedures reasonably designed to ensure that their associated persons who participate in social media sites for business purposes are appropriately supervised . . . and do not present undue risks to investors.”<sup>4</sup> Further, broker-dealers “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.”<sup>5</sup> FINRA expects firms to satisfy these regulatory obligations through the use of software platforms, such as those offered by Socialware Inc. and Smarsh Inc. These platforms usually allow firms to monitor, approve, reject and alter information posted on social media sites by associated persons.

The SEC has offered similar guidance to registered investment advisors under the Investment Advisers Act of 1940, as amended (the Advisers Act). Noting the increasing, “landscape-shifting” use of social media for business purposes, the SEC has suggested that advisers “adopt, and periodically review the effectiveness of, policies and procedures regarding social media in the face of rapidly changing technology.”<sup>6</sup> An SEC National Examination Risk Alert urged advisers to implement guidelines for the appropriate use of social media, restrictions regarding the social media sites that can be used for business purposes and procedures for monitoring employee social media usage.<sup>7</sup> Registered advisers also are required to capture, retain and preserve business-related records generated via social media.<sup>8</sup>

In light of the above guidance, broker-dealers and registered investment advisers are well-advised to promulgate policies limiting the use of social media, carefully monitor such usage and take appropriate disciplinary action when employees or other associated persons violate applicable company policies.

## National Labor Relations Act and Social Media

Efforts to comply with FINRA and SEC guidance, however, place an employer at risk of violating the National Labor Relations Act (NLRA), particularly as interpreted by the NLRB. In both unionized environments and nonunion workplaces, the NLRB and its general counsel have found social media policies to violate the NLRA by “chilling” protected employee activity and interfering with statutorily protected rights. Among the policies the NLRB has deemed unlawful are ones

“prohibit[ing] the use of the company’s name or service mark outside the course of business,” requiring that employee communications be “appropriate” or “professional” and requiring employees to state that opinions expressed on social media are their own and not the opinions of their employer.<sup>9</sup> This application of the NLRA constrains a broker-dealer’s ability to ensure compliance with FINRA regulations, such as by taking prophylactic steps to ensure associated persons’ personal views or posts are not misconstrued as investor advice.

Take, for example, a financial adviser who posts on Facebook that he “likes” the latest iPhone device. Even if his post has nothing to do with investment advice, and, rather, flows from his love of gadgets, viewers might invest on the misperception that the adviser recommends Apple stock and may blame the broker-dealer if the investment goes awry. The broker-dealer at issue could have prevented this miscommunication by, *inter alia*, prohibiting the adviser from discussing his affiliation with the broker-dealer or the adviser’s job responsibilities when using social media. But according to the NLRB, such a prohibition would have violated the NLRA.<sup>10</sup>

Another source of potential conflict is the NLRA’s prohibition on certain “surveillance” of employee activity, including conduct creating employee “fear that members of management are peering over their shoulders.”<sup>11</sup> This prohibition is in tension with the Advisers Act and FINRA Rules, which require firms to supervise business-related communications regardless of whether these communications occur on work computers or other devices, and to ensure that associated persons’ communications do not pose an undue risk to investors.<sup>12</sup> Yet again, employers are left to wonder whether and to what extent legitimate supervision of employees will be deemed to run afoul of the NLRA.

## State Laws Preventing Access to Employees’ Personal Social Media

A third regulatory regime, that imposed by a growing number of states, poses yet additional obstacles to compliance with FINRA and the Advisers Act. A raft of state laws protecting employee privacy serves to restrict companies’ ability to monitor or supervise the social media activities of their employees.

As of the end of February, 12 states had enacted laws prohibiting employers from requesting and/or requiring that employees or prospective employees provide access to their online social media accounts.<sup>13</sup> Many other

<sup>3</sup> See FINRA, Social Media Web Sites, Regulatory Notice 10-06 (January 2010); FINRA, Social Media Websites and the Use of Personal Devices for Business Communications, Regulatory Notice 11-39 (August 2011). Subsequent guidance has been in line with the 2010 and 2011 notices. See, e.g., FINRA, Targeted Examination Letter, Spot-Check of Social Media Communications (June 2013), available at <http://www.finra.org/Industry/Regulation/Guidance/TargetedExaminationLetters/P282569>.

<sup>4</sup> FINRA, Regulatory Notice 10-06, at 7.

<sup>5</sup> FINRA, Regulatory Notice 11-39, at 7.

<sup>6</sup> SEC, National Examination Risk Alert, Investment Adviser Use of Social Media 1-2 (Jan. 4, 2012), available at <http://www.sec.gov/about/offices/ocie/riskalert-socialmedia.pdf>.

<sup>7</sup> See *id.* at 3, 5.

<sup>8</sup> See *id.* at 3, 5, 7.

<sup>9</sup> NLRB, Report of the Acting General Counsel Concerning Social Media Cases, Advice Memorandum OM 12-31, at 13-15 (Jan. 24, 2012), available at <http://op.bna.com/tpif.nsf/r?Open=m1on-8wypya>.

<sup>10</sup> The NLRB does consider an employer’s legitimate business needs when evaluating the legality of its workplace policies but, to date, the NLRB has offered little guidance on the intersection of legitimate business needs and social media restrictions.

<sup>11</sup> NLRB, Advice Memorandum, *Buel Inc.*, No. 11-CA-22936, at 4 (July 28, 2011), available at [http://op.bna.com/sml.nsf/r?Open=m1on-9gvnzw; Flexsteel Indus., 311 N.L.R.B. 257 \(1993\)](http://op.bna.com/sml.nsf/r?Open=m1on-9gvnzw; Flexsteel Indus., 311 N.L.R.B. 257 (1993)).

<sup>12</sup> See FINRA, Regulatory Notice 10-06; FINRA, Regulatory Notice 11-39; 17 C.F.R. § 275.204-2.

<sup>13</sup> These states are Arkansas, California, Colorado, Illinois, Maryland, Michigan, Nevada, New Jersey, New Mexico, Or-

states are actively contemplating similar measures. These laws effectively prevent companies from supervising employee social media usage and from maintaining copies of any investor-related communications made by employees on social media sites.

Although variations exist from state to state, some states' laws do not provide exemptions to allow companies to comply with FINRA or other regulations. For instance, Oregon's law, Or. Rev. Stat. § 659A.330, makes it *per se* illegal for an employer to "require, request, or suggest" that an employee provide access to social media accounts, with no carve-out for complying with conflicting regulatory obligations. Similarly, in California, FINRA tried, and failed, to convince the Legislature to include an exemption allowing FINRA-regulated companies to proactively monitor employees' social media usage.<sup>14</sup> Broker-dealers operating in such states thus face a Catch-22: Either comply with state laws and risk a FINRA investigation over a failure to monitor/supervise, or comply with the federal regulatory regime and face potential liability for violations of state privacy laws.<sup>15</sup>

### The Path Forward

Given the tangled web of governing authority, broker-dealers and registered investment advisers

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egon, Utah and Washington. See National Conference of State Legislatures, *Employer Access to Social Media Usernames and Passwords*, <http://www.ncsl.org/research/telecommunications-and-information-technology/employer-access-to-social-media-passwords-2013.aspx>. On Jan. 22, 2014, Wisconsin's legislature approved S.B. 223, which is expected to be signed into law by Gov. Scott Walker later this year (see *related article*). Note that New Mexico's law, N.M. Stat. Ann. § 50-4-34, covers *prospective* employees only.

<sup>14</sup> See Letter from FINRA to California Assembly Member Nora Campos (June 19, 2012). FINRA argued that the California statute's existing exemption permitting investigations into "employee violation[s] of applicable laws and regulations" was insufficient to allow broker-dealers to comply with FINRA regulations.

<sup>15</sup> Regulated companies may be tempted to eschew state laws and take the position that these laws are pre-empted by FINRA's federal regulatory regime. A recent decision from the U.S. Court of Appeals for the Ninth Circuit, *McDaniel v. Wells Fargo Investments LLC*, 717 F.3d 668 (9th Cir. 2013), provides a basis for such an assertion. But firms that pursue this course will be at heightened risk of litigation, with all its inherent costs and uncertainties.

should be vigilant in designing and maintaining social media policies for their employees and associated persons. A key first step is to identify the particular rules applicable to a firm given its industry, location and social media usage; only then can the firm make prudent judgment calls to try to balance competing regulatory regimes. Firms are well-advised to obtain input from throughout their organization, including their business, marketing/investor relations, legal, human resources and compliance units, in designing comprehensive programs.

At the same time, industry participants should strongly consider becoming more proactive around these key issues, including coordinating with regulators to obtain clearer and more cogent guidance. FINRA is already aware of the issue and has been lobbying in state capitals to achieve carve-outs as social media password laws are debated. Michigan, Utah and Washington have set benchmarks for acceptable exemption language,<sup>16</sup> and conflicts with state laws largely would be ameliorated if other jurisdictions followed suit. The prospect of winning legislative battles in 47 additional states is highly unlikely, however, making this a less-than-perfect approach for a long-term, definitive solution. And even if such battles could be won, broker-dealers and registered investment advisers still would have to contend with the restrictions imposed by the NLRB.

The optimal resolution would be the creation of a single federal regime that defers to FINRA, the SEC and other financial regulatory authorities wherever conflicts exist. Such a regime could be accomplished through a federal social media privacy statute with clear language exempting the monitoring of personal social media accounts if companies are required to do so under applicable law, and pre-empting any conflicting laws, including the NLRA and state laws. Unfortunately, the pending Social Networking Online Protection Act, which would limit employers' ability to monitor or restrict employee social media usage, does not contain such an exemption. Absent a coordinated policy initiative, regulated firms thus may end up with yet another conflicting law with which they must contend.

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<sup>16</sup> See Mich. Comp. Laws § 37.275; Utah Code Ann. § 34-48-202; Wash. Rev. Code § 49.44.200.