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## *SEC Brings Two More “AI Washing” Enforcement Actions Against Investment Advisers, Continuing Its Pursuit of Misstatements Related to AI*

MARCH 27, 2024

On March 18, 2024, the Securities and Exchange Commission (SEC or the Commission) announced settled charges against two investment advisers, Delphia (USA) Inc. and Global Predictions, Inc., for making false and misleading statements about their use of artificial intelligence (AI).<sup>1</sup> Delphia and Global Predictions agreed to settle the SEC’s charges and pay civil monetary penalties of \$225,000 and \$175,000, respectively.<sup>2</sup>

The settled actions are the latest in the SEC’s focus on “AI washing,” or firms’ overstating of their use of AI to attract investors. The SEC previously settled an enforcement action against Rockwell Capital Management LLC<sup>3</sup> and issued an investor alert relating to this conduct.<sup>4</sup> Given the SEC’s focus in this area, firms—not solely investment advisers—should be mindful of statements about their use of AI.

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<sup>1</sup> *SEC Charges Two Investment Advisers with Making False and Misleading Statements About Their Use of Artificial Intelligence*, U.S. SEC. AND EXCH. COMM’N (Mar. 18, 2024), available at [https://www.sec.gov/news/press-release/2024-36?utm\\_medium=email&utm\\_source=govdelivery](https://www.sec.gov/news/press-release/2024-36?utm_medium=email&utm_source=govdelivery) (Press Release).

<sup>2</sup> *Id.*

<sup>3</sup> Complaint, *Sec. and Exch. Comm’n v. Sewell*, No. 1:24-cv-00137-UNA (D. Del. 2024) at 11, available at <https://www.sec.gov/files/litigation/complaints/2024/comp-pr2024-13.pdf>.

<sup>4</sup> *Artificial Intelligence (AI) and Investment Fraud: Investor Alert*, U.S. SEC. AND EXCH. COMM’N (Jan. 25, 2024), available at <https://www.investor.gov/introduction-investing/general-resources/news-alerts/alerts-bulletins/investor-alerts/artificial-intelligence-fraud>.

## *The Delphia and Global Predictions Settlements*

According to the SEC’s order, Delphia, a Toronto-based investment adviser, made false and misleading statements regarding its use of AI in its Form ADV Part 2A brochures, in a press release and on its website.<sup>5</sup> For example, Delphia claimed in a December 2019 press release that it was “the first investment adviser to convert personal data into a renewable source of investable capital . . . that will allow consumers to invest in the stock market using their personal data.”<sup>6</sup> According to the order, Delphia’s website also claimed that the firm “turns [customer] data into an unfair investing advantage” and that Delphia “put[s] collective data to work to make our artificial intelligence smarter so it can predict which companies and trends are about to make it big and invest in them before everyone else.”<sup>7</sup> According to the SEC’s order, these statements were false and misleading because Delphia had not actually developed the represented AI capabilities.<sup>8</sup> As a result of its conduct, Delphia violated Sections 206(2)<sup>9</sup> and 206(4) of the Investment Advisers Act (Advisers Act), as well as Advisers Act Rules 206(4)-1<sup>10</sup> and 206(4)-7.<sup>11</sup> Delphia agreed to settle the charges and pay a civil monetary penalty of \$225,000.

According to the SEC’s order, Global Predictions, a San Francisco-based investment adviser, made false and misleading claims on its website and on social media regarding its use of AI.<sup>12</sup> For example, Global Predictions claimed on its website, in emails to clients and on social media that it was the “first regulated AI financial adviser,” while being unable to substantiate that claim.<sup>13</sup> Global Predictions also claimed on its website that its technology incorporated “[e]xpert AI-driven

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<sup>5</sup> *In the Matter of Delphia (USA) Inc.*, Inv. Adv. Act. Rel. No. 6573 (Mar. 18, 2024) at 3, available at <https://www.sec.gov/files/litigation/admin/2024/ia-6573.pdf>.

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* at 3–4.

<sup>9</sup> Section 206(2) of the Advisers Act makes it unlawful for any investment adviser, directly or indirectly, to “engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client.” Scienter is not required in order to establish a violation of Section 206(2), but rather a violation may rest on a finding of negligence. *SEC v. Steadman*, 967 F.2d 636, 643 n.5 (D.C. Cir. 1992) (citing *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S.180, 195 (1963)).

<sup>10</sup> Section 206(4) of the Advisers Act and Rule 206(4)-1 thereunder prohibit any registered investment adviser from, directly or indirectly, disseminating any advertisement that, among other things, includes any untrue statement of material fact, or omits to state a material fact necessary in order to make the statement made, in the light of the circumstances under which it was made, not misleading or include information that would reasonably be likely to cause an untrue or misleading implication or inference to be drawn concerning a material fact relating to the investment adviser.

<sup>11</sup> Rule 206(4)-7 under the Advisers Act requires, among other things, that a registered investment adviser adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the Rules adopted thereunder.

<sup>12</sup> *In the Matter of Global Predictions, Inc.*, Inv. Adv. Act Rel. No. 6574 (Mar. 18, 2024) at 3, available at <https://www.sec.gov/files/litigation/admin/2024/ia-6574.pdf>.

<sup>13</sup> *Id.*

forecasts” despite not doing so.<sup>14</sup> As a result of the company’s conduct, the order states that Global Predictions violated Sections 206(2) and 206(4) of the Advisers Act, as well as Advisers Act Rules 206(4)-1(a), 206(4)-1(b), 206(4)-1(d) and 206(4)-7. Global Predictions agreed to settle the charges and pay a civil monetary penalty of \$175,000.

## *SEC’s Focus on “AI Washing”*

The SEC’s focus on AI washing is not new; as noted above, the Commission previously settled an action for this conduct and warned investors about this activity. In February 2024, the SEC settled an action against Rockwell Capital Management LLC and its founder for, among other things, claiming that the firm would use proprietary algorithms, including AI and a machine learning model, to monitor and execute orders on global crypto asset exchanges.<sup>15</sup> In January 2024, the SEC’s Office of Investor Education and Advocacy issued an Investor Alert about AI and investment fraud.<sup>16</sup> The alert cautioned investors to be wary of claims from investment firms and professionals regarding investment returns “guaranteed” by AI.<sup>17</sup>

In a press release accompanying the actions against Delphia and Global Predictions, SEC Chair Gary Gensler stated that AI washing “hurts investors” and that “[i]nvestment advisers should not mislead the public by saying that they are using an AI model when they are not.”<sup>18</sup> In a video statement posted on X (formerly Twitter), Gensler elaborated that “AI washing, whether it’s by financial intermediaries such as investment advisers and broker-dealers or by companies raising money from the public . . . may violate the securities laws.”<sup>19</sup> This echoes remarks made during Gensler’s speech in February 2024 at Yale Law School, stating that “[i]nvestment advisers or broker-dealers should not mislead the public by saying that they are using an AI model when they are not, nor say they are using an AI model in a particular way but not do so.”<sup>20</sup>

Gurbir Grewal, Director of the SEC’s Division of Enforcement, stated in the Commission’s press release for the Delphia and Global Predictions settlements that the SEC is “committed to protecting

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<sup>14</sup> *Id.*

<sup>15</sup> Complaint, *Sec. and Exch. Comm’n v. Sewell*, No. 1:24-cv-00137-UNA (D. Del. 2024) 53–54, available at <https://www.sec.gov/files/litigation/complaints/2024/comp-pr2024-13.pdf>.

<sup>16</sup> *Artificial Intelligence (AI) and Investment Fraud: Investor Alert*, U.S. SEC. AND EXCH. COMM’N (Jan. 25, 2024), available at <https://www.investor.gov/introduction-investing/general-resources/news-alerts/alerts-bulletins/investor-alerts/artificial-intelligence-fraud>.

<sup>17</sup> *Id.*

<sup>18</sup> Press Release.

<sup>19</sup> Gary Gensler (@GaryGensler), X (Mar. 18, 2024, 8:11 AM), <https://twitter.com/GaryGensler/status/1769698079333130684>.

<sup>20</sup> Chair Gary Gensler, “AI, Finance, Movies, and the Law” Prepared Remarks before the Yale Law School (Feb. 13, 2024), available at <https://www.sec.gov/news/speech/gensler-ai-021324>.

[investors] against those engaged in ‘AI washing.’”<sup>21</sup> In an accompanying video statement posted on X, Grewal stated that the actions against Delphia and Global Predictions “should serve notice to the investment industry that if you claim to use AI in your investment processes, you must ensure that your representations aren’t false [or] misleading.”<sup>22</sup>

## *Looking Forward*

The actions against Delphia and Global Predictions indicate that the SEC will continue its focus on AI washing. However, there is nothing new or novel about the violations, which relate to inaccurate or misleading disclosures. Much like “green washing,” where companies and financial institutions overstate their sustainability practices in public disclosures, AI washing is just the latest area where the SEC is focusing on the inaccurate or misleading statements made by firms.<sup>23</sup>

During the Securities Industry and Financial Markets Association (SIFMA) Compliance and Legal Conference on March 18, 2024, Grewal remarked that the SEC is technology-agnostic but will continue to pursue actions for traditional misconduct that involves technology, such as misstatements and breaches of fiduciary duties by investment advisers related to advances in technology.

As investor interest in AI continues to grow, firms may wish to capitalize on that interest by expanding their use of AI technologies. When doing so, firms should be mindful of the SEC’s actions in this area and accurately describe their use of AI in a way that reflects their AI capabilities and practices. Notably, to date the SEC has solely brought actions against investment advisers for AI washing, although as indicated by Chair Gensler in his February 2024 speech at Yale, the SEC has authority to bring actions for misstatements brought by all firms subject to its jurisdiction, including public companies and broker-dealers.<sup>24</sup> As a result, all firms and persons subject to SEC jurisdiction should also be mindful of their AI-related statements and disclosures.

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<sup>21</sup> Press Release.

<sup>22</sup> U.S. Securities and Exchange Commission (@SECGov), X (Mar. 18, 2024, 8:07 AM), <https://twitter.com/SECGov/status/1769697224613597285>.

<sup>23</sup> See, e.g., Complaint, *Sec. and Exch. Comm’n v. Vale S.A.*, No. 1:22-cv-02405 (E.D.N.Y. 2022), available at <https://www.sec.gov/files/litigation/complaints/2022/comp-pr2022-72.pdf> (charging issuer with, among other things, making inaccurate statements in its environmental, social and governance disclosures in violation of Section 17(a) of the Securities Act); *In the Matter of Credit Suisse Securities (USA) LLC*, Sec. Act Rel. No. 10013 (Jan. 31, 2016) (charging firm with, among other things, making inaccurate statements in its order handling disclosures in violation of Section 17(a) of the Securities Act).

<sup>24</sup> *Id.*

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