



Financial Industry Regulatory Authority

**Joseph P. Savage**  
Vice President & Counsel  
FINRA Office of General Counsel

April 12, 2021

Ms. Vanessa Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

**Via Email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov)**

**Re: File No. SR-FINRA-2020-038 -- Proposed Amendments to FINRA Rules 5122 (Private Placements of Securities Issued by Members) and 5123 (Private Placements of Securities) That Would Require Members to File Retail Communications Concerning Private Placement Offerings That Are Subject to Those Rules' Filing Requirements (the "Proposal")**

Dear Ms. Countryman:

This letter is being submitted by the Financial Industry Regulatory Authority, Inc. ("FINRA") in response to a comment letter from Mick Law P.C., L.L.O. ("Mick") received by the Securities and Exchange Commission ("SEC" or "Commission") on February 2, 2021, regarding the above-referenced rule filing. The Proposal would amend FINRA Rules 5122 (Private Placements of Securities Issued by Members) and 5123 (Private Placements of Securities) to require members to file retail communications that promote or recommend private placement offerings that are subject to those rules' filing requirements.<sup>1</sup>

As FINRA discussed in both its initial response to comments dated January 12, 2021,<sup>2</sup> and its second response to comments dated January 29, 2021,<sup>3</sup> the Commission published the Proposal for public comment in the Federal Register on November 6,

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<sup>1</sup> See Securities Exchange Act Release No. 90302 (November 2, 2020), 85 FR 71120 (November 6, 2020) (Notice of Filing of File No. SR-FINRA-2020-038).

<sup>2</sup> See Letter from Joseph P. Savage, FINRA, to Vanessa Countryman, Secretary, SEC, dated January 12, 2021 ("Initial Response").

<sup>3</sup> See Letter from Joseph P. Savage, FINRA, to Vanessa Countryman, Secretary, SEC, dated January 29, 2021 ("Second Response").

2020, and the public comment period expired on November 27, 2020. The Commission initially received five comment letters directed to the rule filing, to which FINRA responded in the Initial Response. The Commission subsequently received a comment letter from the Institute for Portfolio Alternatives (“IPA”) on January 26, 2021 (“IPA Comment Letter”), to which FINRA responded in the Second Response.

On February 4, 2021, the Commission issued an order instituting proceedings to determine whether to approve or disapprove the Proposal.<sup>4</sup> Although Mick filed its comment letter two days prior to the Commission’s order instituting proceedings, FINRA will take this opportunity to respond to the comments in its letter. No comment letters or rebuttals were filed with the Commission following the February 4, 2021, order.

Mick states that it is a law firm that provides due diligence legal counsel and underwriting to broker-dealers, registered investment advisers, and other firms, and assist firms in their evaluations of the features and risks of alternative investments marketed through private placements. As part of this process, Mick assists its clients with reasonable basis suitability reviews of programs to help clients fulfill their investigative obligations under the federal securities laws and FINRA rules.

Mick states that it routinely reviews private placement memoranda, websites and retail communications of sponsors seeking to raise capital for various private offerings. Mick further states that it has encountered many instances in which a sponsor’s website or other offering promotional materials were not in compliance with FINRA Rule 2210 (Communications with the Public). Mick states that the most pervasive rule infractions it has encountered are unsubstantiated presentations of forecasts, the lack of prominent risk disclosures, and improper comparisons of securities products.

Mick states that, while it sympathizes with FINRA’s concerns related to private placement advertising, it supports comments made in the IPA Comment Letter that many sponsors and broker-dealers misunderstand what types of “economic result” related content are permitted under Rule 2210. Mick references an example in the IPA letter relating to a program’s cash flow, and queries whether it is permissible to refer to

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<sup>4</sup> See Securities Exchange Act Release No. 91066 (February 4, 2021), 86 FR 8970 (February 10, 2021) (Notice of Filing of Amendment No. 1 and Order Instituting Proceedings to Determine Whether to Approve or Disapprove the Proposed Rule Change, as Modified by Amendment No. 1, to FINRA Rules 5122 (Private Placements of Securities Issued by Members) and 5123 (Private Placements of Securities) That Would Require Members To File Retail Communications Concerning Private Placement Offerings That Are Subject to Those Rules’ Filing Requirements).

a program's budgeted cash flow as a "return target" or "return objective" if it is accompanied by disclosure concerning the risks of not achieving this target or objective. Mick also states that it would welcome a clarification of what types of "operating metrics" information would be permitted if it is reasonably explained and accompanied by disclosure.

As we discussed in the Second Response, Mick's comments, like the IPA Comment Letter, concern how FINRA applies Rule 2210 rather than the filing requirements of FINRA Rules 5122 and 5123. The Proposal would amend Rules 5122 and 5123 to require members to file retail communications that recommend or promote private placement offerings that are subject to those rules' filing requirements. The Proposal would not amend or provide guidance on Rule 2210. Given that Mick's and the IPA's comments concern only Rule 2210 and do not address the Proposal's substance, FINRA does not believe that the Commission should base its decision of whether to approve the Proposal on comments regarding a separate rule.

Mick's primary concern appears to be how FINRA has interpreted the prohibitions on performance projections. Subject to specified exceptions,<sup>5</sup> Rule 2210(d)(1)(F) prohibits member communications from predicting or projecting performance or making any exaggerated or unwarranted claim, opinion or forecast. As discussed in Regulatory Notice 20-21, retail communications<sup>6</sup> concerning private placements may not project or predict returns to investors such as yields, income, dividends, capital appreciation percentages or any other future investment performance.<sup>7</sup>

However, FINRA would not consider reasonable forecasts of issuer operating metrics (e.g., forecasted sales, revenues, or customer acquisition numbers) that may convey important information regarding the issuer's plans and financial position to be inconsistent with the rule. These presentations should provide a sound basis for evaluating the facts, such as clear explanations of the key assumptions underlying the

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<sup>5</sup> There are four exceptions from the prohibition on projections: hypothetical illustrations of mathematical principles, investment analysis tools, price targets in research reports, and specified projections concerning security futures and options. See FINRA Rules 2210(d)(1)(F), 2215(b)(3), and 2220(d)(3).

<sup>6</sup> FINRA Rule 2210(a)(5) defines a "retail communication" as any written (including electronic) communication that is distributed or made available to more than 25 retail investors within any 30 calendar-day period. A retail investor is any person other than an institutional investor, regardless of whether the person has an account with a FINRA member. See FINRA Rule 2210(a)(6).

<sup>7</sup> See Regulatory Notice 20-21 at page 4.

forecasted issuer operating metrics and the key risks that may impede achievement of the forecasted metrics.<sup>8</sup>

For example, in reviewing past retail communications concerning private placements as part of a member firm examination, or that were filed with FINRA, FINRA staff has not considered a retail communication that shows a private real estate investment program's future contractual rental income and estimated future expenses, or that presents the program's estimated future net operating income, to be inconsistent with Rule 2210. Unfortunately, some member firms have attempted to use this information to create projected or targeted rates of return to investors, or projected income per share in the program. Rule 2210(d)(1)(F) precludes member firms from using the data from forecasts of issuer operating metrics to project or depict specific investment returns to an investor. FINRA clearly articulated this interpretation of Rule 2210 in Regulatory Notice 20-21.

Mick also states that private placement marketing material may present "distribution rates" within retail communications. Mick gives as an example where a program's earnings have exceeded its distribution rate on an audited basis over a period of two or more years and asks whether it is permissible to present this as a "statement of fact" within the retail communication. Mick further inquires whether the presence of additional risk disclosures explaining the applicable market risks and uncertain nature of the asset's future returns would help to make such an assertion permissible.

Regulatory Notice 20-21 provides detailed guidance regarding the use of distribution rates in retail communications concerning private placements. If a member firm has a question regarding a specific private placement offering retail communication that it is considering for use, the member is welcome to file the retail communication with FINRA's Advertising Regulation Department for review.<sup>9</sup> In addition, the staff has been and will continue to be willing to discuss issues regarding

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<sup>8</sup> Id. In 2017, FINRA solicited comment on proposed amendments to Rule 2210 that would create an exception to the rule's prohibition on projecting performance to permit a member to distribute a customized hypothetical investment planning illustration that includes the projected performance of an asset allocation or other investment strategy, but not an individual security, subject to specified conditions. See Regulatory Notice 17-06 (February 2017). FINRA is still considering potential amendments to the prohibition of projections as part of future proposed rule amendments.

<sup>9</sup> Information about filing communications with the Advertising Regulation Department can be found at <https://www.finra.org/rules-guidance/key-topics/advertising-regulation/about>.

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particular retail communications that are filed with FINRA with member firms and their counsel both before and after a communication is filed.

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FINRA believes that the foregoing responds to the material issues raised by Mick's comment letter. Accordingly, FINRA respectfully requests that the SEC approve the Proposal on or prior to February 4, 2021. If you have any questions, please contact me at [REDACTED].

Best regards,

/s/ Joseph P. Savage

Joseph P. Savage  
Vice President & Counsel  
FINRA Office of General Counsel