



Financial Industry Regulatory Authority

Joseph P. Savage
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January 29, 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

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 the Institute for Portfolio Alternatives ("IPA") received by the Securities and Exchange Commission ("SEC" or "Commission") on January 26, 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.¹

As FINRA discussed in its initial response to comments dated January 12, 2021,² the Commission published the Proposal for public comment in the Federal Register on November 6, 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 IPA's comment letter

¹ 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).

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

was filed on January 26th, nearly two months after the Federal Register comment period closed. The IPA's late comments should not delay the Commission's approval of the proposed rule change.

Additionally, as discussed below, the IPA's comments concern how FINRA applies FINRA Rule 2210 (Communications with the Public) rather than the filing requirements of Rules 5122 and 5123. The Proposal would amend FINRA 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 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.

The IPA's primary concern appears to be how FINRA has interpreted the prohibitions on performance projections. Subject to specified exceptions,³ 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 communications⁴ 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.⁵

However, FINRA does allow retail communications concerning private placements to include 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. These presentations should provide a sound basis for evaluating the facts, such as clear explanations of the

³ 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).

⁴ 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).

⁵ See Regulatory Notice 20-21 at page 4.

key assumptions underlying the forecasted issuer operating metrics and the key risks that may impede achievement of the forecasted metrics.⁶

Contrary to the IPA's claims, FINRA has not interpreted Rule 2210 to prohibit firms promoting private offerings from disclosing estimated future expenses associated with an investment program. In fact, in many cases, such information would be required to balance the presentation or provide material information pursuant to Rule 2210(d)(1)(A).

For example, in the past FINRA has permitted members to show a private real estate investment program's future contractual rental income and estimated future expenses, and to present the program's estimated future net operating income. 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. When operating data is used to create projections of an investment's returns to investors, FINRA considers such projections to be inconsistent with Rule 2210(d)(1)(F). FINRA clearly articulated this interpretation of Rule 2210 in Regulatory Notice 20-21.

Finally, FINRA disagrees with the assertion that it does not provide any guidance regarding its principles-based content standards, such as the requirement that member communications be fair and balanced and not misleading.⁷ For many years, FINRA has issued guidance on these requirements in specific contexts, whether through Notices, interpretive letters, FAQs, and more informal guidance provided at FINRA conferences as well as via direct conversations with members. This guidance has included Notices that address retail communications concerning how FINRA interprets Rule 2210's content standards with regard to real estate investment programs and other private placement offerings.⁸

⁶ 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 these or future proposed rule amendments.

⁷ See FINRA Rule 2210(d)(1)(A) and (B).

⁸ See, e.g., Regulatory Notice 10-22 (April 2010), Regulatory Notice 13-18 (May 2013), and Regulatory Notice 20-21 (July 2020).

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FINRA believes that the foregoing responds to the material issues raised by the IPA'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 (240) 386-4534, email: joe.savage@finra.org.

Best regards,

/s/ Joseph P. Savage

Joseph P. Savage
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