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June 11, 2025

By email to pubcom@finra.org

Jennifer Piorko Mitchell
Office of the Corporate Secretary
Financial Industry Regulatory Authority, Inc.
1700 K Street, NW
Washington, DC 20006

RE: Regulatory Notice 25-04: *Rule Modernization*;
Regulatory Notice 25-06: *Supporting Capital Formation*

Dear Ms. Mitchell:

On behalf of the North American Securities Administrators Association, Inc. ("NASAA"),[1] I am writing in response to Financial Industry Regulatory Authority, Inc. ("FINRA") Regulatory Notice 25-04: *Rule Modernization* and Regulatory Notice 25-06: *Supporting Capital Formation*,[2] which seek commentary to inform FINRA's "broad review of its regulatory requirements applicable to member firms and associated persons." While NASAA may comment on specific proposals if and when they are issued by FINRA, we offer the following general principles to help guide FINRA's review. First, the prospective modernization of FINRA rules should be narrow and targeted, and should prioritize investor protection. Second, FINRA should work to promote *responsible* capital formation by maintaining rules for oversight of private offerings and those promoting them.

I. The modernization of FINRA rules should be narrow and targeted, and should prioritize investor protection.

In the two Notices, FINRA seeks comments broadly on how its rules might be modernized in light of other regulatory schemes that apply to FINRA member firms and broader developments in the markets, products, services, and technology. The two initial areas of focus identified in Regulatory Notice 25-04 – capital formation and the modern workplace – implicate a wide array of important rules and guidance designed to protect investors and the markets from fraud and

[1] Organized in 1919, NASAA is the oldest international organization devoted to investor protection. NASAA's membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, México, Puerto Rico, the U.S. Virgin Islands, and Guam. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

[2] Regulatory Notice 25-04; Regulatory Notice 25-06.

abuse.[3] Therefore, it is imperative that any adjustments in these areas be narrow, targeted, and precise. Where possible, revisions should be informed by empirical data through mechanisms like compliance inspections, examination sweeps, and properly-designed pilot programs, rather than bare FINRA member firm preferences and speculation.

FINRA should also avoid rule changes that favor certain technologies, products, services, or business models at the expense of investor protection. NASAA has consistently advocated for stronger requirements to ensure that developments in products, practices, and technology do not leave investor protection considerations behind.[4] Unfortunately, the two Notices appear to invite such a result by unduly favoring the reduction of regulatory requirements over the investor protection benefit of existing FINRA rules. Technologies like artificial intelligence, distributed ledger technology, and new web and mobile applications can help to expand participation in our capital markets, but they come with risks. Many of these risks are familiar, despite new technological wrappers, but emerging technologies can exacerbate existing risks or change the manner in which they materialize.[5]

FINRA should therefore avoid changes that favor emerging technologies, products, services, or business models, or otherwise allow them to operate outside of existing safeguards that have been carefully designed to protect investors from well-understood risks of fraud and abuse. Instead, FINRA should continue to apply well-established principles to protect investors from similar risks, regardless of the technology or investment product, and FINRA member firms should continue to focus first on their duties to investors when providing new trading tools, services, and products. For example, we believe that existing rules already cover most digital engagement practices and technology-based recommendations and investment advice.[6] However, we believe that FINRA has not paid sufficient attention to parsing the circumstances in which these practices are and are not recommendations, and that this gap should not be further exacerbated in

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[3] *See* Regulatory Notice 25-04 at 3-4.

[4] *See* Letter from Melanie Senter Lubin, NASAA President and Maryland Securities Commissioner, to Jennifer Piorko Mitchell, FINRA Office of the Corporate Secretary, Re: Regulatory Notice 22-08: *Complex Products and Options* (May 9, 2022); Letter from Melanie Senter Lubin, NASAA President and Maryland Securities Commissioner, to Vanessa Countryman, Secretary, SEC, Re: File No S7-10-21: *Request for Information and Comments on Broker-Dealer and Investment Adviser Digital Engagement Practices, Related Tools and Methods, and Regulatory Considerations and Potential Approaches; Information and Comments on Investment Adviser Use of Technology to Develop and Provide Investment Advice* (the "DEP Comment Letter") (Oct. 1, 2021); Letter from Christopher Gerold, NASAA President and Chief, New Jersey Bureau of Securities, to Vanessa Countryman, Secretary, SEC, Re: File No. S7-24-15: *Use of Derivatives by Registered Investment Companies and Business Development Companies; Required Due Diligence by Broker-Dealers and Registered Investment Advisers Regarding Retail Customers' Transactions in Certain Leveraged/Inverse Investment Vehicles* (Mar. 27, 2020); Letter from Christopher Gerold, NASAA President and Chief, New Jersey Bureau of Securities, to Jennifer Piorko Mitchell, FINRA Office of the Corporate Secretary, Re: Regulatory Notice 19-27: *Retrospective Rule Review* (Oct. 8, 2019).

[5] *See* Daryl Tarver et al., *White Collar Alert: SEC roundtable presents both risks and opportunities of AI in the financial industry*, DLA Piper (Apr. 3, 2025).

[6] *See* DEP Comment Letter, *supra* note 4.

the face of continuing technological advancement.[7] We recommend that FINRA strengthen the existing framework by providing guidance about when these practices are recommendations and requiring FINRA member firms to understand and disclose the limits and potential conflicts of these innovations to their customers.

II. FINRA should work to promote *responsible* capital formation by maintaining rules for oversight of private offerings and those promoting them.

FINRA should exercise particular care when considering updates to its rules concerning oversight of the private securities markets, with respect to both private offerings themselves and the people and firms promoting them. Regulatory Notice 25-06 asks whether FINRA should create a "tailored rule set" for ostensibly limited-purpose broker-dealers, including finders.

As NASAA has cautioned in the past when opposing proposals to carve finders out of the existing regulatory framework, the private markets are known to be prone to abuse.[8] State securities regulators frequently see fraud and other harms where unregistered persons promote unregistered investments to retail investors.[9] While data about the private markets remains limited, a staff white paper published by the SEC's Division of Economic and Risk Analysis noted that "offerings linked to SEC enforcement actions more likely involved an unregistered intermediary or a recidivist, or solicited from unsophisticated investors."[10] This is consistent with the experience

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[7] *See*, *e.g.*, Robert W. Cook, Statement Before the Financial Services Committee U.S. House of Representatives (May 6, 2021) (noting that "a broker-dealer's customer interface that promotes trading activity . . . is also *potentially subject to Reg BI, depending on the facts and circumstances*" (emphasis added)); Sarah Aberg & Shane Killeen, *Game On: FINRA Hints at Upcoming Gamification Sweep*, Sheppard Mullin, Corporate & Securities Law Blog (June 2, 2021) (noting that "speakers [at FINRA's annual conference] indicated that any future rulemaking, guidance or regulatory action [by FINRA] regarding gamification would be undertaken in conjunction with the [SEC]").

[8] *See* Letter from Lisa Hopkins, NASAA President and General Counsel and Senior Deputy Commissioner of Securities, West Virginia, to Vanessa Countryman, Secretary, SEC, Re: File No. S7-13-20: *Notice of Proposed Exemptive Order Granting Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Finders*, at 2-3 (the "Finders Comment Letter") (Nov. 12, 2020).

[9] *See*, *e.g.*, Summary Cease and Desist and Penalty Order, *Akintunde S. Akinniyi and Ace FX Partners LLC* (N.J. Bur. of Sec., Feb. 21, 2024) (finding that unregistered person engaged in fraud in the sale of unregistered securities in forex trading and training business); Findings of Fact, Conclusions of Law, and Final Order to Cease and Desist and Order Awarding Civil Penalties, Costs, and Restitution, *Retire Happy, LLC et al.*, Case No. AP-20-06 (Mo. Office of Sec. of State, Mar. 10, 2021) (determining that respondents committed fraud in connection with the offer and sale of unregistered securities without being licensed); Final Order, *Cannacea, LLC and Tisha Siler*, Case No. S-16-0007 (Ore. Dept. of Consumer and Bus. Servs., Div. of Fin. Reg., Sept. 21, 2017) (finding fraud in the sale of unregistered investments in marijuana dispensary).

[10] Rachita Gullapalli, SEC Division of Economic and Risk Analysis, Misconduct and Fraud in Unregistered Offerings: An Empirical Analysis of Select SEC Enforcement Actions, 33 (Aug. 2020).

of state securities regulators.[11] The staff also observed that studies indicate that "fraud is more likely to occur when there are fewer outside gatekeepers like underwriters, analysts and regulators."[12] Given the experiences of state securities regulators, available evidence, and the obvious dangers of combining unregistered promoters with unregistered offerings, this is not an area where regulatory safeguards should be weakened.

Controls such as licensing, registration, and examination or inspection serve essential gatekeeper functions, and FINRA rules impose additional controls on broker-dealers for good reason. This includes rules requiring firms and associated persons to adhere to a high standard of conduct, supervise their activities effectively, know their customers, understand the products they are selling, and keep and maintain records to ensure that regulators have the information they need to fulfill their roles. As FINRA President and CEO Robert Cook has aptly stated,

> [an] advantage that has traditionally been identified is that SROs can raise the standard of conduct in the industry. This benefit is most apparent in the ethical requirements and detailed business conduct rules that an SRO can establish that extend beyond the realm of federal law. These standards can deter dishonest and unfair practices that might not amount to fraud, but nonetheless can undermine investor confidence and compromise capital formation.[13]

FINRA should not back away from these important controls or otherwise take steps to weaken its role in the oversight of its members' activities in the private markets.

Regulatory Notice 25-06 further asks whether FINRA should reconsider certain aspects of FINRA Rule 2310 and requests suggestions for exemptions that FINRA should consider from the

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[11] *See*, *e.g.*, Summary Revocation Order, *Carlos Leston a/k/a Jose Carlos Leston a/k/a Jose C. Leston (CRD No. 3021614)* (N.J. Bur. of Sec., Sept. 30, 2024) (finding that agent engaged in dishonest or unethical practices by, *inter alia*, acting as an unregistered finder for company at which his friend served as CEO, and selling investments in the company to two elderly clients, including recommending that the clients surrender annuities to fund the purchase); Petition for Permanent Injunction and Other Relief, *Okla Dept. of Sec. v. Premier Global Corp. et al.*, Case No. CJ-2022-5066 (Okla. Cnty. Dist. Ct., Oct. 13, 2022) (alleging fraud in connection with the offer and sale of unregistered securities by unregistered agents, including individuals who had previously been the subjects of securities regulatory enforcement actions); Notice of Agency Action and Order to Show Cause, *Fred M. Randhahn, CRD#1338801*, Docket No. SD-21-0006 (Utah Div. of Sec., Mar. 26, 2021) (alleging fraud in the sale of $625,000 of unregistered Woodbridge securities as finder, without approval by employing broker-dealer); *Retire Happy (Mo. Office of Sec. of State)*, *supra* note 9 (finding fraud in connection with the sale of unregistered securities by unlicensed entity and individuals); Desist and Refrain Order, *Retire Happy, LLC et al.* (Cal. Dept. of Fin. Protection and Innovation, Mar. 24, 2023) (finding fraud in connection with the offer and sale of at least $1.5 million of securities to California investors); Order to Cease and Desist and Order to Show Cause Why Civil Penalties, Restitution, Costs and Other Administrative Relief Should Not Be Imposed, *John D. Myers et al.*, Case No. AP-21-02 (Mo. Office of Sec. of State, Feb. 23, 2021) (alleging fraud in the sale of unregistered securities by unregistered finder).

[12] Gullapalli, *supra* note 10, at 10 (citing academic studies).

[13] Robert W. Cook, Remarks: New Special Study Conference, Columbia University, New York, NY (Mar. 24, 2017) (emphasis added).

requirements of FINRA Rules 5122 and 5123. FINRA should exercise caution in these areas as well.

FINRA Rule 2310 establishes certain suitability, disclosure, and other requirements that must be met before a FINRA member firm may participate in a public offering of certain direct participation programs. These products are typically expensive, illiquid, and involve a greater degree of risk than other publicly offered investments. Given the complexity of these products, FINRA member firms serve an important gatekeeper function when offering and selling them, particularly to retail investors.[14] State securities enforcement actions over the years have demonstrated the investor harm that can occur when firms do not adequately fulfill this role.[15] As such, we believe that the requirements and protections established in Rule 2310 remain both important and relevant to protect investors, and this too is an area where regulatory safeguards should not be weakened.

For private placements of securities issued by FINRA member firms, FINRA Rule 5122 currently requires that the firm provide basic disclosures, file the relevant offering documents and any retail communications (*i.e.*, advertisements) about the offering with FINRA, and requires that the firm actually use a certain portion of the offering proceeds for business purposes. For other private placements, FINRA Rule 5123 requires only that a FINRA member firm file the offering documents and advertisements with FINRA, or tell FINRA that no offering documents or advertisements were used. Both rules include specified exemptions, including for offerings sold only to types of investors who could plausibly be considered sophisticated enough to fend for themselves. The requirements in these rules are basic and commonsense, and they serve an important purpose that facilitates continued trust in our capital markets.[16] FINRA should be skeptical of comments suggesting that these rules serve as barriers to capital formation.

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[14] *See* Gullapalli, *supra* note 10, at 10 (citing studies suggesting that "fraud is more likely to occur when there are fewer outside gatekeepers").

[15] *See*, *e.g.*, Administrative Complaint, *Charles C. Kulch*, Docket No. E-2017-0079 (Mass. Sec. Div., July 16, 2020) (alleging that agent "effected unsuitable non-traded REIT transactions in the accounts of dozens of Massachusetts investors" and violated firm procedures); Consent Order, *NEXT Financial Group, Inc.*, Docket No. E-2017-0079 (Mass. Sec. Div., Dec. 20, 2019) (alleging that the firm failed to supervise non-traded REIT sales by its agent); Consent Order, *Va. State Corp. Comm. v. LPL Financial LLC*, Case No. SEC-2015-00052 (May 26, 2017) (alleging that the firm failed to supervise its agents in connection with the sale of non-traded REITs in excess of the REITs' prospectus standards, applicable state concentration limits, or the firm's internal guidelines); Consent Order, *Ameriprise Financial Services, Inc.*, Order No. S-14-1575-16-CO02 (Wash. Dept. of Fin. Inst., May 18, 2016) (finding that the firm made unsuitable recommendations to older investors to purchase non-traded REITs, failed to supervise its salesperson, and failed to comply with FINRA Rule 2310); Consent Order, *John Charles Hanson*, Order No. S-14-1592-15-CO01 (Wash. Dept. of Fin. Inst., Jan. 4, 2016) (finding fraud in the form of, *inter alia*, the offer and sale of a fictitious REIT investment).

[16] *See* Letter from Lisa Hopkins, NASAA President and General Counsel and Senior Deputy Commissioner of Securities, West Virginia, to J. Matthew DeLesDernier, Assistant Secretary, SEC, Re: File No. SR-FINRA-2020-038: *Notice of Filing of 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*

More specifically, skepticism is warranted for any suggestion that FINRA exempt, or loosen requirements for, offerings sold solely to natural person accredited investors from its rules. As NASAA has explained in the past, the current income and net worth criteria for "accredited" status are not an effective proxy for financial sophistication, especially since they have not been meaningfully updated since 1982.[17] Even the most sophisticated investors will struggle to make sound investment decisions if they are given bad recommendations or deprived of material information. Indeed, NASAA has consistently urged policymakers to enhance, not weaken, protections in the private markets by providing better and more timely information to investors, firms, and regulators.[18] We therefore urge FINRA not to weaken Rule 2310 or discard the fundamental oversight and modest regulatory burden under Rules 5122 and 5123 for private offerings sold to these investors.

III. Conclusion

NASAA appreciates the opportunity to comment on Regulatory Notice 25-04 and Regulatory Notice 25-06 and to contribute to FINRA's review of its rules. Thank you for considering these views. Should you have any questions about this letter, please contact either the undersigned or NASAA's General Counsel, Vince Martinez, at (202) 737-0900.

Sincerely,

Leslie M. Van Buskirk

Leslie M. Van Buskirk
NASAA President and
Administrator, Division of Securities
Wisconsin Department of Financial Institutions

(Nov. 24, 2020) (supporting FINRA's proposed revision of the rules to require the filing of advertisements, which some firms were already doing without an explicit requirement).

[17] *See*, *e.g.*, Written Testimony of Amanda W. Senn, Director, Alabama Securities Commission and 2024-2025 NASAA Enforcement Section Co-Chair, before the House Comm. on Fin. Servs., at 19-22 (Mar. 25, 2025); Letter from Joseph Brady, NASAA Executive Director, to Rep. French Hill, Chairman, and Rep. Maxine Waters, Ranking Member, House Comm. on Fin. Servs., at 2 (Feb. 25, 2025); Letter from Joseph Brady, NASAA Executive Director, to Sen. Charles Schumer et al., at 13 (June 15, 2023); Letter from Andrew Hartnett, NASAA President and Deputy Commissioner, Iowa Insurance Division, to Erik F. Gerding, Director, Div. of Corp. Fin., SEC, Re: *Private Market Reforms*, at 4-5 (Mar. 7, 2023); Finders Comment Letter, *supra* note 8, at 6-7.

[18] *See*, *e.g.*, Letter from Leslie M. Van Buskirk, NASAA President and Administrator, Division of Securities, Wisconsin Dept. of Fin. Inst., to Svent Bossart, Clerk, House Comm. on Fin. Servs., Re: March 25, 2025, Hearing, "Beyond Silicon Valley: Expanding Access to Capital Across America" (Apr. 29, 2025) (discussing proposed draft legislation to empower market stakeholders with earlier and better information that would benefit regulators, lawmakers, investors, and companies seeking capital).