
SECURITIES LAW UPDATE April 22, 2010

**FINRA Issues Guidelines Regarding Broker-Deal Responsibilities
in Private Offerings**

The Financial Industry Regulatory Authority (FINRA) has issued guidance for FINRA-registered firms reminding them of their “substantial” responsibilities regarding investor suitability, adequacy of disclosure and other requirements for selling private placements, including PIPEs. According to FINRA, recent examinations and enforcement actions by both the SEC and FINRA have revealed a significant lack of broker-dealer compliance with existing rules. FINRA has commenced several enforcement actions recently and the indication is that it will continue to investigate and bring enforcement actions in this area against member firms who are not fulfilling all of their obligations in connection with the sale of securities in private offerings.

FINRA recently undertook a nationwide initiative that has involved active examinations and investigations of broker-dealers engaged in sales of private placement interests. According to FINRA, that initiative has uncovered misconduct, including fraud and sales practice abuses. Recent problems uncovered by FINRA in Reg D offerings have resulted in firms being sanctioned for providing private placement memoranda and sales materials to investors that contained inaccurate statements or omitted information necessary to make informed investment decisions.

Under FINRA rules and regulations, the broker-dealer bears responsibility for conducting adequate due diligence to ensure that the statements made by the issuer in a private placement memorandum or other offering materials complies with the anti-fraud provisions of the Securities Act. This is not a dischargeable duty that rests solely with the issuer.

Under FINRA Regulatory Notice 10-22, broker-dealers are required to conduct a reasonable investigation of an issuer and its securities before recommending private placements made under Regulation D of the Securities Act of 1933.

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Moreover, beyond merely determining that an investor is an “accredited investor”, as defined in Rule 501 of Regulation D, broker-dealers are required to conduct reasonable investigations into whether the private placements they recommend are suitable investments for a particular client. In addition, the broker-dealer must ensure that the customer fully understands the risks involved in the investment.

Broker-dealers offering securities in private placements also must comply with FINRA advertising, supervisory and record-keeping rules. Finally, broker-dealers offering securities in Reg D private placements must adhere to FINRA Rule 2010, requiring just and equitable principles of trade, as well as FINRA Rule 2020, which prohibits manipulative and fraudulent devices.

If you have questions regarding the FINRA guidance, practice tips or specific fact patterns, please contact:

Lance Jon Kimmel
SEC Law Firm
11693 San Vicente Boulevard
Suite 357
Los Angeles, CA 90049
Tel. 310/557-3059
lkimmel@seclawfirm.com