

FINRA Regulatory Notice 10-22 Compliance Checklist

Regional Center Project Name: _____

Investigation

A. Antifraud Provisions and FINRA Rules

- Disclosed lack of essential information as well as the risks that arise from lack of information
- Exercised a high degree of care in investigating and independently verifying an issuer's representations and claims
- Regarding new speculative ventures, was particularly careful in verifying the issuer's obviously self-serving statements

B. FINRA Suitability Obligations

- Had reasonable grounds to believe that a recommendation to purchase, sell or exchange a security is suitable for the customer
- Conducted a suitability analysis when recommending securities to both accredited and non-accredited investors that will take into account the investors' knowledge and experience
- Made reasonable efforts to gather and analyze information about the customer's other holdings, financial situation and needs, tax status, investment objectives and such other information that would enable the firm to make its suitability determination
- Is satisfied that the customer fully understands the risks involved and is able to take those risks

Conducted, at a minimum, a reasonable investigation concerning:

- the issuer and its management;
 - the business prospects of the issuer;
 - the assets held by or to be acquired by the issuer;
 - the claims being made; and
 - the intended use of proceeds of the offering.
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- Conducted a reasonable investigation in connection with each offering, notwithstanding that a subsequent offering may be for the same issuer

C. Specific Issues Related to a BD's Responsibilities

- Identified and conducted independent investigation of any red flags
- Identified and conducted further, independent investigation of substantial adverse information about the issuer
- Disclosed adverse information about issuer
- Disclosed conflicts of interest where present between broker/dealer and customer
- Carefully reviewed the qualifications and competency of counsel or experts retained to perform an investigation on its behalf
- Separately addressed all gaps or omissions in the investigation by counsel or experts
- Conducted further investigation of issues and concerns identified in the counsel's or expert's report

D. Supervision

Firm ensured that the firm's personnel, including its registered representatives:

- Engaged in an inquiry that is sufficiently rigorous to comply with their legal and regulatory requirements
- Performed the analysis required by NASD Rule 2310
- Qualified their customers as eligible to purchase securities offered pursuant to Regulation D
- Did not violate the antifraud provisions of the federal securities laws or FINRA rules in connection with their preparation or distribution of offering documents or sales literature

E. Documentation of Reasonable Investigation

Descriptions of the meetings that were conducted in the course of the investigation, including meetings with the issuer or other parties, showing:

- tasks performed the documents and other information reviewed
- results of such reviews,
- date such events occurred
- individuals who attended the meetings or conducted the reviews.

Reasonable Investigation Practices

A. Issuer and Management

- Examined the issuer's governing documents, including any charter, bylaws and partnership agreement, noting particularly the amount of its authorized stock and any restriction on its activities. If the issuer is a corporation, a broker/dealer might determine whether it has perpetual existence
- Examined historical financial statements of the issuer and its affiliates, with particular focus, if available, on financial statements that have been audited by an independent certified public accountant and auditor letters to management
- Looked for any trends indicated by the financial statements
- Inquired about the business of affiliates of the issuer and the extent to which any cash needs or other expectations for the affiliate might affect the business prospects of the issuer
- Inquired about internal audit controls of the issuer
- Contacted customers and suppliers regarding their dealing with the issuer
- Reviewed the issuer's contracts, leases, mortgages, financing arrangements, contractual arrangements between the issuer and its management, employment agreements and stock option plans
- Inquired about past securities offerings by the issuer and the degree of their success while keeping in mind that simply because a certain product or sponsor historically met obligations to investors, there are no guarantees that it will continue to do so, particularly if the issuer has been dependent on continuously raising new capital
- Inquired about pending litigation of the issuer or its affiliates
- Inquired about previous or potential regulatory or disciplinary problems of the issuer
- Requested credit check of the issuer

Made reasonable inquiries concerning the issuer's management, including:

- Expertise of management for the issuer's business
 - The extent to which management has changed or is expected to change
 - Any regulatory or disciplinary history on the part of management
 - Any loans or other transactions between the issuer or its affiliates and members of management that might be inappropriate or might otherwise affect the issuer's business
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- Inquired about the forms and amount of management compensation, who determines the compensation and the extent to which the forms of compensation could present serious conflicts of interest
 - Inquiring about the length of time that the issuer has been in business and whether the focus of its business is expected to change

B. Issuer's Business Prospects

Reasonable investigations of the issuer's business prospects, and the relationship of those prospects to the proposed price of the securities being offered, might include:

- Inquired about the viability of any patent or other intellectual property rights held by the issuer
- Inquired about the industry in which the issuer conducts its business, the prospects for that industry, any existing or potential regulatory restrictions on that business and the competitive position of the issuer
- Requested any business plan, business model or other description of the business intentions of the issuer and its management and their expectations for the business
- Analyzed management's assumptions upon which any business forecast is based
- Tested models with information from representative assets to validate projected returns, break-even points and similar information provided to investor

- Requested financial models used to generate projections or targeted returns
- Maintained in the BD's files a summary of the analysis that was performed on financial models provided by the issuer that detailed the results of any stress tests performed on the issuer's assumptions and projections

C. Issuer's Assets

- Visited and inspected a sample of the issuer's assets and facilities
- Determined whether the value of assets reflected in the financial statements are reasonable
- Determined that management's assertions concerning the condition of the issuer's physical plants and the adequacy of its equipment are accurate
- Carefully examined any geological, land use, engineering or other reports by third-party experts that may raise red flags
- Obtained, with respect to energy development and exploration programs, expert opinions from engineers, geologists and others are necessary as a basis for determining the suitability of the investment prior to recommending the security to investors
- Adopted practices specifically tailored to current offering to ensure adequate investigation