

Fintech Focus: FINRA Publishes Supervisory Expectations for Crypto Asset Retail Communications

Publications

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In recent guidance, the Financial Industry Regulatory Authority (FINRA) published the results of its targeted examination or “sweep” of crypto assets retail communications distributed or issued by its member firms, finding that 70% of the sampled communications contained potential violations of FINRA Rule 2210, which requires communication with the public to be fair and balanced, among other things. In issuing this guidance, FINRA outlined questions firms should be asking themselves—and that FINRA will itself ask in an examination—when they engage in such communications.

FINRA’s definition of crypto assets (also known as digital assets) encompasses all “assets that are issued or transferred using distributed ledger or blockchain technology.” While many crypto assets are not securities, and therefore do not directly fall under FINRA’s purview, the sale of or engagement in crypto assets as a business line by a FINRA member firm brings that activity well within FINRA’s jurisdiction. Similarly, pursuant to FINRA’s crypto assets guidance, a registered representative’s engagement in crypto assets business as an outside business activity or as private securities transactions (to the extent a crypto asset is deemed a security or a related transaction is deemed a securities transaction) can raise supervisory and/or reporting obligations for the member firm. As such, FINRA member firms are expected to properly supervise their crypto assets business to ensure that this specific area of their business complies with applicable FINRA rules, including FINRA Rule 2210. FINRA Rule 2210 governs communication with the public and prohibits, among other things, the publication of inaccurate or misleading information. The rule also requires that communications to the public related to products and services be fair and balanced and free of false, exaggerated, misleading claims.

What did FINRA’s sweep cover?

FINRA’s sweep focused on its member firms’ practices surrounding “retail communications concerning crypto asset products and services” during the period from July 1, 2022, through September 30, 2022. In connection with this sweep, FINRA asked the subject member firms to provide certain pieces of information, including, among other things:

1. A copy of all crypto asset retail communications including the date the communication was first available to the public;
2. Whether the communication was filed with FINRA's Advertising Regulation Department;
3. Whether a principal of the firm had reviewed and approved each communication. If so, FINRA requested the approval date;
4. Written policies and procedures, and all guidance (including training materials) governing crypto asset retail communication; and
5. Contracts between the member firm and its affiliates or third parties concerning crypto assets or products or services relating to crypto assets including agreements and processes relating to the creation and dissemination of crypto asset retail communications.

While the requests are not out of the ordinary for an examination, they provide insight into the types of questions FINRA would ask during a routine examination, the focus of its reviews, and FINRA's expectations of its member firms in terms of documentation and record retention in connection with their crypto assets communications.

What were the sweep's findings?

In finding that 70% of the sampled communications contained potential violations of FINRA Rule 2210, FINRA identified violations involving inaccurately characterizing crypto assets as functioning like cash or cash equivalents; failing to clearly disclose material information relating to crypto assets including how they operate (e.g. "how [they] are issued, held, transferred, or sold"), their features and associated risks; failing to provide a sound basis for comparisons between crypto assets and other investments (e.g., stocks or gold); misleading statements concerning whether crypto assets are protected by Securities Investor Protection Corporation (SPIC) or under Securities Investor Protection Act (SIPA); and misrepresentation of the applicability of federal securities laws and FINRA rules to crypto assets.

What insights does this sweep offer member firms?

While the sweep does not provide new expectations relating FINRA Rule 2210, it clearly draws a picture of FINRA's expectations of its member firms in terms of how the rule applies to crypto asset retail communication, including the expected supervisory, governance, and record retention framework that FINRA member firms should have in place. Specifically:

- Firms are expected to have adequate policies and procedures governing communication with the public and this expectation extends to crypto asset retail communication.
- Crypto asset retail communication distributed by an associated person as part of their private securities business can raise supervisory obligations on their FINRA member firm.

- Firms must retain their communications relating to crypto assets, and the communication must be subject to the firm’s supervisory review and approval process in compliance with FINRA Rule 2210.
- Communication relating to crypto assets must be free of unwarranted or misleading content. Statements about crypto assets that FINRA may deem misleading include:
 - describing them as easily tradable liquid assets,
 - overstating their safety,
 - inaccurately representing, explicitly or implicitly, that they are secured or backed by another entity (e.g., a clearing firm or a trading platform), or
 - misleadingly comparing them or their benefits to other assets such as gold or cash alternatives.
- FINRA expects firms to affirmatively disclose lack of SIPC or SIPA protections when applicable.
- Firms should also affirmatively disclose whether the crypto assets referenced in the communication are being offered by the firm, its affiliate, or a third party.
- The communication must fairly describe the risks of crypto assets, including disclosing the lack of legal or regulatory protections where applicable.
- The communication should be clear relating to fees and commissions associated with crypto assets.

So, what does the sweep mean for FINRA member firms?

This latest publication is not the first piece of guidance that FINRA has issued relating to crypto assets, but it does provide further insight into the sorts of conduct that are likely to raise concerns for FINRA. It expands on prior crypto assets related notices and guidance by FINRA, including a dedicated “Crypto Assets Key Page”, and has specifically included crypto asset developments in its 2024 Priorities Report. As such, FINRA member firms can expect crypto assets to continue to be an examination focus and priority during FINRA examinations and can expect crypto assets retail communications, specifically, to be subject to the regulator’s scrutiny.

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