



Association for Corporate Growth

Congress Codifies M&A Broker Exemption

▲ Clarity Brings New Opportunities

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Panel - M&A Broker Registration Exemption



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Agenda - M&A Broker Registration Exemption

- Overview – what Congress changed (effective last March 29th)
 - Impacts – federal securities broker-dealer regulation
 - Impacts – states' securities broker-dealer regulation
 - No impacts – other state-level licensing laws
- Clarity brings new opportunities for deal flow –
 - Transaction-based compensation (success fees) – registered and exempt firms
 - Compensated referrals – “right-sizing” professional staffing
 - Restructuring registered corporate finance broker-dealers' business models
- Panel discussion – multiple firms' perspectives
- Q&A

Overview – How we got here

- **2005 – American Bar Association, Business Law Section, publishes Private Placement Broker-Dealer Report**
- 2006 - AM&AA, IBBA, and M&A Source engage WNJ as securities counsel to develop and advocate for exemption
- 2006 – SEC Country Business, Inc. (CBI) No Action Letter
- 2006 to 2012 – Parallel regulatory paths with both SEC staff and North American Securities Administrators Association
- **2013 – 2014 H.R. 2274 M&A broker legislation introduced and unanimously passes full U.S. House (but not Senate)**
- **2014 – SEC staff M&A Brokers no action letter (M&AB NAL) issued to six ABA securities lawyers 2 weeks later**
- 2015 – 2016 H.R. 686 M&A broker legislation reintroduced but not taken up by House or Senate
- **2015 – North American Securities Administrators Association (NASAA) state model M&AB exemption rule published**
- 2017 – 2018 H.R. 477 M&A broker legislation reintroduced and unanimously passes full U.S. House (but not Senate)
- 2019 – H.R. 609 M&A broker legislation reintroduced – passes full U.S. House as/in three different bills (but not Senate)
- 2021 – H.R. 935 M&A broker legislation reintroduced and unanimously passes full U.S. House
- 2022 – H.R. 2617, Senate attaches and passes H.R. 935 in Consolidated Appropriations Act, 2023, Division AA, Title V
- **2022 – President Biden signs the Consolidated Appropriations Act, 2023 into law on December 29, 2022**

Overview - M&A Brokers Exemption

- Amended the Securities and Exchange Act of 1934 by
 - Adding new M&A Brokers registration exemption in Section 15(b)(**13**)
 - Qualifying private company in M&A securities deals
 - FINRA registration/licenses no longer required in M&A securities transactions
 - **BUT Capital-raising** still requires registration as/with a B-D
 - Largely codifies the 2014 SEC staff M&AB NAL (with the SEC's tacit support)
 - SEC withdrew its M&AB NAL on March 29, 2023 (effective date of the new exemption)
 - Federal securities laws still apply to securities transactions
 - SEC jurisdiction and all anti-fraud prohibitions are unaffected
 - Issuers' private offering registration exemptions' requirements are unaffected
 - State(s) securities and other state(s) licensing laws still apply

Notes:

M&A Brokers Registration Exemption

- Who is an “M&A broker” under the new exemption?
 - A [securities] “**broker**” – any person engaged in the business of effecting transactions involving securities for the account of others
 - “**M&A broker**” includes any **broker** (including “associated persons”)
 - Engaged in the business of . . .
 - Effecting securities transactions solely in connection with . . .
 - The transfer of ownership of . . .
 - An “eligible privately held company” through . . .
 - The purchase, sale, exchange, issuance, repurchase, or redemption of, or a business combination involving . . .
 - Securities or assets of the eligible privately held company, if the broker reasonably believes [three things] . . .
- M&A broker must “reasonably believe” 3 things –
 - Only Florida law requires seller and buyer’s written assurances
 - E.g., Cover this in the M&AB’s client engagement and evidenced in deal dox
 - After closing, buyer will **hold a controlling interest**; AND
 - Presumption of control at 25% or more (non-exclusive)
 - After closing, buyer will be **active in post-closing management** (directly/indirectly)
 - **If** seller is **offered buyer’s securities** (e.g., equity rollovers) (i.e., seller will be an investor)
 - Buyer must provide seller at/prior to offer of its securities
 - Buyer’s last FY financial statements
 - Buyer’s current (w/in 120 days) balance sheet
 - Buyer’s MD&A of last FY’s performance
 - Buyer’s material loss contingencies
 - So, the securities analysis of the buyer’s form of consideration is very important
 - E.g., “earn-outs”, “seller’s notes”, equity rollovers, options, warrants

M&A Brokers Registration Exemption

- Scope – applies to private company M&A transactions
 - Target - “eligible privately held company”
 - Cannot sell/buy SEC-registered securities
 - No “pink sheets” public companies
 - Alternative target company size caps:
 - **\$250 million** in “book” gross revenues; **and/or**
 - **\$25 million** in “book” EBITDA
 - Metrics apply to fiscal year ended prior to M&A broker’s engagement
 - Metrics apply to target’s actual FY financial statements (no adjustments)
 - Target must be an operating company, not a “shell company”
 - E.g., target cannot be a “special purpose acquisition company” (SPAC)
 - Tax-related M&A-specific subsidiaries for forward/reverse triangular sub mergers are OK
- Six Conditions to the exemption – **M&AB can’t do’s**
 - Cannot have **custody**, possession or control of deal’s funds or securities
 - Use third-party escrow services for earnest money
 - Reminder – only applies in M&A securities transactions
 - Cannot be **engaged in public offering** of securities
 - A public company can be a buyer, but not in a public offering
 - Cannot provide deal financing (directly or indirectly)
 - PE/VC firms can be a buyer or seller, but
 - PE/VC firms cannot charge M&A broker’s success fees on portfolio company deals
 - Cannot be involved in a sale to passive buyers
 - Cannot form or facilitate forming a group of buyers
 - SEC concerns with M&A broker’s creating a private fund comprised of passive buyers
 - SEC focused on PE firm/fund charging success fees on portfolio company deals
 - Cannot use a power of attorney to bind a seller or buyer

M&A Brokers Registration Exemption

- Permissible activities – **M&AB can do's**
 - Can be engaged by either seller or buyer
 - Can be a “neutral” broker with disclosure/consent
 - Can assist with obtaining third-party financing with –
 - Disclosure of role and relationships (and related conflicts of interest)
 - Disclosure of any related third-party compensation
 - Doesn't cover capital-raising activities or related compensation
 - Structure/timing of M&A Broker's compensation is not limited
 - E.g., can be a combination of cash and equity interests
 - No prescribed recordkeeping requirements
 - But think defensively – how to prove it if necessary
- Disqualifications –
 - M&A brokerage firm, owners, and management –
 - Cannot be barred from the securities industry
 - Cannot be suspended from securities registration
 - Subject to some state-level disqualification types (e.g., state licensing violations)

Notes:

What about FINRA registration and regulation?

- SEC-registered B-Ds must be an “SRO” member
 - SRO = a “self-regulatory organization”
 - Financial Industry Regulatory Authority (FINRA) is the default SRO
 - FINRA’s jurisdiction only applies to its members and registered professionals
- SEC registration/FINRA membership is still required for -
 - Securities deals outside the scope of the M&A brokers registration exemption
 - Public offerings of SEC-registered stock/securities
 - Capital-raising from passive investors in any capacity (e.g., a “finder”)
 - Fairness opinions, among other securities activities
- **If FINRA-registered**, FINRA rules **still apply** including –
 - Rule 2210 *Communications with the Public*
 - Advertising, teasers, CIMs, pitchbooks, etc.
 - Rule 2040 *Payments to Unregistered Persons*
 - General prohibition against sharing regulated comp; **but**
 - M&AB registration exemption allows paying/sharing M&A deal compensation sharing
 - Rule 3270 *Outside Business Activities* (OBAs)
 - Registered professionals must give OBA notice to B-D
 - OBAs are reported on Form U4 and often B-D firm’s forms
 - OBAs are publicly visible on FINRA BrokerCheck (<https://brokercheck.finra.org/>)
 - Rule 3280 *Private Securities Transactions* (PSTs)
 - PSTs = securities transactions not conducted through the B-D
 - Registered professionals must receive B-D’s approval; **and**
 - B-D must supervise that PST securities transaction
 - Supervision similar but not necessarily the same as its own deals
 - Some B-Ds may charge for Rule 3280 supervision in view of their potential liabilities

What about state securities regulation?

20 states have adopted M&A-specific exemptive relief (other exemptions may be available):

- **Alaska** Rule 45.56.420 Registration Exemption for Merger and Acquisition Broker (2019-01-22)
- **Arkansas** Rule 302.01, Merger Acquisition Broker Exemption (2020-10-05)
- **Colorado** Rule 51-3.33 Licensing Exemption for Merger and Acquisition Brokers (2017-07-15)
- **Florida (law)** Section 517.12(22)(a) Merger and Acquisition Broker Exemption (2017-09-07)
- **Georgia** M&A Broker No-Action Letter (2015-01-23)
- **Illinois** Section 130.830 Registration Exemption for M&A Brokers (2016-11-30)
- **Iowa** Section 191-50.10(502) Broker-Dealer Registration - Exemptions (2018-05-08)
- **Maryland** Order - M&A Broker Dealer (2017-12-07)
- **Michigan** Rule 4.2 Merger and Acquisition Broker Exemption (2019-07-03)
- **Mississippi** Rule 5.35 Registration Exemption for Merger and Acquisition Brokers (2018-06-03)
- **Montana** Rule 6.10.308 Merger and Acquisition Broker Exemption (2020-10-24)
- **Nebraska** Interp. Opinion No. 19 – Merger & Acquisition Brokers (2019-08-09)
- **Oklahoma** Rule 660 11-5-26 Merger and Acquisition Broker Exemption (2020-11-01)
- **Pennsylvania** - M&A Broker No-Action Letter (2016-01-25)
- **South Carolina** - M&A Broker No-Action Letter (2014-11-12)
- **South Dakota** Rule 20.08.03.18 Business Brokers (2019-02-18)
- **Tennessee** Securities Bulletin - M&A Brokers (2017-09-11)
- **Texas** Rules Section 139.27 M&A Dealer Exemption (2016-02-25)
- **Utah** Policy Position Letter - M&A and Business Broker (2014-02-28)
- **Vermont** Section 3-4 Registration Exemption for M&A Broker Dealers (2016-11-21)

What about other state-level licensing?

- Real estate and business broker licensing –
 - Continues without change by the new federal law
 - Most states require real estate licensing
 - Some states require business broker licensing
 - Some states combine these licenses into one licensing regime
 - State laws apply to both securities-registered and exempt firms/individuals
 - An estimated 15 states have M&A-related real estate/biz broker licensing exemptions for persons registered as or with an SEC/FINRA broker-dealer
 - State real estate/biz broker licensing is beyond the scope of this presentation

Panel – clarity brings new opportunities

- Transaction-based M&A compensation – registered and exempt firms
 - Qualifying private company M&A transactions – less than either:
 - \$250 Million prior FY gross revenue (actual); and/or
 - \$25 Million prior FY EBITDA (actual)
- Compensated referrals – “right-sizing” a deal’s professional staffing
 - Down-stream compensated M&A deal referrals
 - Up-stream compensated M&A deal referrals
 - M&A broker networking and deal marketing
- Networking and marketing M&A brokerage services
- Restructuring registered corporate finance broker-dealers’ business models
 - Push qualifying private company M&A deals into an unregistered M&A broker affiliate

Industry Reference Resources


For more detailed information and latest updates visit these websites:

- **Business Intermediary Education Fund (BIEF)**
<http://www.biefoundation.org>
- **Alliance of Merger & Acquisition Advisors (AM&AA)**
<https://amaaonline.com/campaign-for-clarity/>
- **International Business Brokers Association (IBBA)**
<https://www.ibba.org/resource-center/legal-updates/>
- **M&A Source (M&AS)**
<https://masource.org/resources/legal-updates/>

BIEF Campaign for Clarity - Contribution

Contribute on-line: <https://www.biefoundation.org/contribute-bief/>

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