
February 7, 2014

SEC Provides Relief from Broker-Dealer Registration for Private M&A Brokers

The Securities and Exchange Commission's Division of Trading and Markets has granted no-action relief that would allow brokers in private M&A transactions to avoid registration as broker-dealers under Section 15(b) of the Securities Exchange Act of 1934, so long as certain conditions are met. This most recent guidance broadens the relief that existed under prior no-action letters, which was limited in its usability by M&A brokers, because, among other things, it was restricted generally to transactions that did not involve securities transfers, larger (non-small business) entities or partial sales and also prohibited certain broker activities and compensation.

The Division's no-action relief will now permit M&A brokers¹ to engage in the following activities, without Section 15 registration:

- Represent a buyer, seller or both, but the broker may represent both only if he or she discloses clearly, in writing, to both parties as to which parties he or she represents and obtains written consent from both parties to any joint representation;
- Facilitate a transaction for any size privately held target;
- Advertise a company for sale, so long as there is no public offering of securities;
- Participate in deal negotiations;
- Advise the parties to issue securities or otherwise to effect the transfer of the business by means of securities, or assess the value of any securities sold; and
- Receive transaction-based or other compensation, as agreed by the parties.

Conditions to the above relief include the following:

- The transaction may involve only targets that are privately held (*i.e.*, companies that do not have any class of securities registered, or required to be registered, with the SEC under Section 12 of the Exchange Act, or with respect to which the company makes or is required to make periodic filings under Section 15(d) of the Exchange Act);

¹ Defined as persons "engaged in the business of effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company. . . through the purchase, sale, exchange, issuance, repurchase, or redemption of, or a business combination involving, securities or assets of the company, to a buyer that will actively operate the company."

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- Targets must be operating companies that are going-concerns. A “going concern” does not have to be profitable and may even be emerging from bankruptcy, but it must have actually been conducting business (which may include soliciting or effecting business transactions and R&D activities);
 - No party to any transaction may be a shell company, other than a business combination related shell company. What constitutes a shell company or a business combination related shell company is similar to definitions found in existing federal securities rules, including Rule 405 of the Securities Act of 1933 and Rule 12b-2 of the Securities Exchange Act of 1934. A shell company is one that has (i) no or nominal operations and (ii) no or nominal assets, assets consisting solely of cash and cash equivalents or assets consisting of any amount of cash and cash equivalents and nominal other assets. A “business combination related shell company” is one that is formed by an entity that is not a shell company solely for the purpose of (i) changing the corporate domicile of that entity solely within the United States or (ii) completing a business combination transaction among one or more entities other than the shell company, none of which is a shell company;
 - The transaction may not involve a public offering. Any offering or sale of any securities must be conducted in compliance with an applicable exemption from registration under the Securities Act of 1933, and any securities received by the buyer or broker in the transaction will be restricted securities pursuant to Rule 144(a)(3) of the Securities Act;
 - The buyer, or buyer group, will, upon completion of the transaction, control and actively operate the company or the business conducted with the assets of the business. No transaction may result in the transfer of interests to any passive buyers. “Control” is defined as having the power, directly or indirectly, to direct the management or policies of a company (through ownership of securities, by contract or otherwise), and necessary control is presumed to exist if, upon completion of the transaction, the buyer or buyer group has the right to vote, or to sell or direct the sale of, 25% or more of a class of voting securities; or in the case of a partnership or limited liability company, has the right to receive upon dissolution, or has contributed, 25% or more of the capital; and
 - The broker may not:
 - Have the ability to bind a party to a transaction;
 - Directly or indirectly provide financing for the transaction, although he or she may assist buyers in obtaining financing from unaffiliated third parties in compliance with all applicable legal requirements (including Regulation T) if he or she discloses any compensation in writing to the client;
 - Have custody, control, or possession of or otherwise handle funds or securities issued or exchanged in connection with the transaction or other securities transaction for the account of others;
 - Facilitate a transaction with a group of buyers unless the group is formed without the assistance of the broker; or

- Have been barred from association with a broker-dealer by the SEC, any state or any self-regulatory organization; or suspended from association with a broker-dealer.

The no-action letter specifically states that relief is limited to the SEC's broker-dealer registration requirements and not other provisions of the federal securities laws (including applicable anti-fraud provisions) or state or other registration requirements. For a copy of the no-action letter, click [here](#).

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Justin G. Hamill
212-373-3189
jhamill@paulweiss.com

Jeffrey D. Marell
212-373-3105
jmarell@paulweiss.com

Robert B. Schumer
212-373-3097
schumer@paulweiss.com

Frances F. Mi
212-373-3185
fmi@paulweiss.com