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November 19, 2018

The Honorable Jeb Hensarling
Chairman
House Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Maxine Waters
Ranking Member
House Committee on Financial Services
4340 O'Neil Federal Office Building
Washington, D.C. 20024

Re: H.R. 6127, the "Unlocking Capital for Small Businesses Act of 2018"

Dear Chairman Hensarling and Ranking Member Waters:

On behalf of the North American Securities Administrators Association ("NASAA"),[1] I am writing to express concern regarding H.R. 6127, the "Unlocking Capital for Small Businesses Act of 2018," which was recently introduced in the House and referred to the Committee on Financial Services.

The Unlocking Capital for Small Businesses Act of 2018 would amend Section 15 of the Securities Exchange Act of 1934 to exempt "private placement brokers" from the registration requirements applicable to broker-dealer representatives under existing federal securities laws. The bill would also establish a regulatory "safe harbor" for so-called "finders," which the bill defines to include persons earning up to $500,000 annually in transaction-based compensation from the sale of privately offered securities.[2] While H.R. 6127 would provide the U.S. Securities and Exchange Commission ("SEC") with statutory authority to adopt new and less stringent regulations for private placement brokers not covered by the bill's safe harbor, the bill would preempt the authority of states to enforce any law, rule, or requirement that exceeds federal requirements for any person acting as either a private placement broker or finder as defined in the bill.[3]

NASAA shares Congress's interest in expanding access to capital for small and growing businesses; however, as described below, H.R. 6127 would have the opposite effect. Furthermore, NASAA strongly opposes any effort to prevent state regulators from protecting investors in the private placement marketplace.

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1 The oldest international organization devoted to investor protection, the North American Securities Administrators Association, Inc. was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

2 The term "private placement broker" typically describes a person who act as a broker of privately issued securities while the term "finder" may be used to describe an intermediary who assists a broker in identifying accredited investors who may purchase the securities. While the term "finder" is sometimes applied to persons serving as intermediaries whose compensation is not derived from the sale of securities, for purposes of H.R. 6127, the term is defined as encompassing only persons who "receive transaction-based compensation."

3 The bill provides that the SEC shall adopt rules for private placement brokers that are "no more stringent than those imposed on funding portals, as defined in section 304 of the Jumpstart Our Business Startups Act of 2012." The bill also directs the SEC to adopt regulations requiring FINRA to provide "reduced membership requirements" for persons covered by the bill. Additional information about the registration requirements for funding portals is accessible at https://www.sec.gov/divisions/marketreg/tmcompliance/cfintermediaryguide.htm#requirements-for-intermediaries.

Significant differences certainly exist in the functions commonly associated with traditional broker-dealer representatives, private placement brokers, and finders. However, such differences do not support exempting these individuals from regulatory oversight or less meaningful registration requirements. To the contrary, the securities laws correctly recognize that individuals who receive compensation directly tied to the sale of securities are functioning as securities brokers regardless of any actual or apparent differences in services or functions performed by particular securities salespersons and promoters.

As an initial matter, the definitions of private placement brokers and finders in H.R. 6127 are overly broad and fail to impose meaningful limitations on the scope of their exemption from registration. Indeed, the bill in its present form would create a loophole in the law that could function as a safe harbor for securities brokers to act in a host of new capacities including, potentially, their engagement in activities beyond the scope of services traditionally performed by finders. The bill also includes provisions that would authorize such private placement brokers and finders to "self-certify" their compliance with the bill's requirements and relevant SRO rules for the purposes of entering into legally binding contracts for activities, such as the promotion and sale of securities.

Furthermore, even if H.R. 6127 is amended to more appropriately limit the scope of the exemption and limited registration requirements applicable to finders and private placement brokers, respectively, Congress would be ill-advised to pass legislation that would preclude the appropriate oversight of persons acting as private placement brokers or finders in this way. Similarly, Congress would be profoundly mistaken to enact legislation that would limit or impair the authority of states to conduct oversight of these or other persons operating as securities brokers within their jurisdiction.

In considering legislative proposals relating to the oversight of private placement brokers and finders, Congress should also scrutinize the practical implications of such policies based on the size and nature of the U.S. private securities marketplace more broadly. The private placement marketplace is large, expanding, and already minimally regulated. Moreover, there is a well-documented relationship between private offerings sold by brokers and an elevated risk of fraud. Indeed, many persons acting as brokers in the private offering marketplace are brokers with red flags in their record.[4] Such overwhelming evidence that bad practices are already more prevalent among brokers engaged in the sale of private placement offerings fails to support the premise that actors in these markets should be subject to less oversight.

Thank you for your consideration of NASAA's views. If I may be of any further assistance, please do not hesitate to contact me or Michael Canning, NASAA's Director of Policy and Government Affairs, at (202) 737-0900.

Sincerely,

Michael Pieciak
NASAA President and Vermont Commissioner of Financial Regulation

[4] For example, based on a 2018 analysis performed by the Wall Street Journal, one in eight brokers marketing private placements in the past decade had three or more red flags on their records, such as an investor complaint, regulatory action, criminal charge, or firing, compared to one in 50 for active brokers. Furthermore, brokers selling private placements are six times more likely as the average broker to have at least one reported regulatory action against them. *See:* Jean Eaglesham and Coulter Jones, *A Private-Market Deal Gone Bad: Sketchy Brokers, Bilked Seniors and a Cosmetologist*, The Wall Street Journal (May 7, 2018).