NOTICE OF REQUEST FOR ADDITIONAL COMMENTS REGARDING A PROPOSED NASAA MODEL RULE EXEMPTING CERTAIN MERGER AND ACQUISITON BROKERS FROM REGISTRATION PURSUANT TO STATE SECURITIES ACTS

NASAA Model Rule Exempting Certain Merger and Acquisition Brokers from State Registration[1]

April 2015

NASAA Comment Period

The NASAA comment period is from April 16, 2015 to May 17, 2015. To facilitate consideration of comments, please send comments to Bryan Lantagne (bryan.lantagne@state.ma.us), Chair of the Broker Dealer Section; Carolyn Mendelson (cmendelson@pa.gov), Chair of the Market Regulatory Project Group; and Christopher Staley (cs@nasaa.org) at NASAA.

We encourage, but do not require, comments to be submitted by e-mail. Hard copy comments may be submitted at the address below.

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Note: After the comment period has closed, NASAA will post to its website the comments it receives as submitted by the authors. Parties should therefore only submit information that they wish to make publicly available. Further, the following notice will appear on NASAA's website where comments are posted: *NASAA, its agents, and employees accept no responsibility for the content of the comments posted on this Web page. The views, expressions, and opinions expressed in the comments are solely those of the author(s).*

Background

The North American Securities Administrators Association ("NASAA") is requesting additional comments to its proposed uniform state model rule ("Proposed Rule") regarding the exemption of certain merger and acquisition brokers ("Merger and Acquisition Brokers") from registration as "brokers," "dealers," "agents," and/or "broker-dealers" pursuant to state securities laws.[2]

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[1] With respect to securities professionals and the firms with which they are associated, some states use the term "licensing" in the same manner as other jurisdictions may use the term "registration." While this Proposed Rule only refers to "registration," for purposes of this Proposed Rule, the two terms should be considered synonymous.
[2] NASAA issued its first request for comments in January 2015.

On January 31, 2014 (as revised on February 4, 2014), the Staff of the United States Securities and Exchange Commission ("SEC") issued a No-Action Letter to Faith Colish, Esq., Martin A. Hewitt, Esq., Eden L. Rohrer, Esq., Linda Lerner, Esq., Ethan L. Silver, Esq., and Stacy E. Nathanson, Esq. ("SEC Letter"). The SEC Letter states that SEC Staff would recommend that no enforcement action be taken against Merger and Acquisition Brokers who: (1) comply with certain conditions enumerated in the SEC Letter; (2) receive transaction-based compensation for facilitating mergers, acquisitions, business sales, and business combinations between sellers and buyers of eligible privately-held companies ("M&A Transactions"); and (3) do not register as broker-dealers with the SEC pursuant to Section 15(b) of the Securities Act of 1934.

In addition to the SEC Letter, prior to 2015, federal legislation has been drafted and/or introduced for consideration by Congress that would exempt Merger and Acquisition Brokers from some of the registration requirements in the federal securities laws. These bills have been broader in the relief granted to Merger and Acquisition Brokers than the SEC Letter.

State securities regulators (the "States") also may decide to exempt Merger and Acquisition Brokers from broker, dealer, broker-dealer, and/or agent registration at the state level[3] for those Merger and Acquisition Brokers who qualify for relief from securities registration pursuant to the SEC Letter or as contemplated by federal legislation. [4]

Text of Model Rule

Rule _____. Registration Exemption for Merger and Acquisition Brokers

(A) IN GENERAL - Except as provided in paragraphs (B) and (C), a Merger and Acquisition Broker shall be exempt from registration pursuant to _____ under this section.

(B) EXCLUDED ACTIVITIES – A Merger and Acquisition Broker is not exempt from registration under this paragraph if such broker does any of the following:

(i) Directly or indirectly, in connection with the transfer of ownership of an eligible privately held company, receives, holds, transmits, or has custody of the funds or securities to be exchanged by the parties to the transaction.

(ii) Engages on behalf of an issuer in a public offering of any class of securities that is registered, or is required to be registered, with the United States Securities and Exchange Commission under Section 12 of the

[3] However, certain states do require registration of business brokers at this time. The terms "broker," "dealer," "broker-dealer," "agent" are defined terms in state securities laws.

[4] This Proposed Rule only exempts Merger and Acquisition Brokers from the registration provisions of state securities laws and not from any other provisions, including the anti-fraud provisions of state securities laws.

Securities Exchange Act of 1934, 15 U.S.C. 78o(b), or with respect to which the issuer files, or is required to file, periodic information, documents, and reports under the Securities Exchange Act of 1934 Section 15(b) subsection (d), 15 U.S.C. 78o(d).

(iii) Engages on behalf of any party in a transaction involving a public shell company.

(C) DISQUALIFICATIONS – A Merger and Acquisition Broker is not exempt from registration under this paragraph if such broker is subject to –

(i) Suspension or revocation of registration under Section 15(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78o(b)(4);

(ii) A statutory disqualification described in section 3(a)(39) of the Securities Exchange Act of 1934, 15 U.S.C. 78c(a)(39);

(iii) A disqualification under the rules adopted by the United States Securities and Exchange Commission under Section 926 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, 15 U.S.C. 77d note; or

(iv) A final order described in paragraph (4)(H) of Section 15(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78o(b)(4)(H).

(D) RULE OF CONSTRUCTION – Nothing in this paragraph shall be construed to limit any other authority of this _____ (Commission, Agency) to exempt any person, or any class of persons, from any provision of this title, or from any provision of any rule or regulation thereunder.

(E) DEFINITIONS – In this paragraph:

(i) CONTROL – The term "control" means the power, directly or indirectly, to direct the management or policies of a company, whether through ownership of securities, by contract, or otherwise. There is a presumption of control for any person who –

(I) is a director, general partner, member or manager of a limited liability company, or officer exercising executive responsibility (or has similar status or functions);

(II) has the right to vote 20 percent or more of a class of voting securities or the power to sell or direct the sale of 20 percent or more of a class of voting securities; or

(III) in the case of a partnership or limited liability company, has the right to receive upon dissolution, or has contributed, 20 percent or more of the capital.

(ii) ELIGIBLE PRIVATELY HELD COMPANY –

(1) IN GENERAL – The term "eligible privately held company" means a company meeting both of the following conditions:

(aa) The company does not have any class of securities registered, or required to be registered, with the United States Securities and Exchange Commission under Section 12 of the Securities Exchange Act of 1934, 15 U.S.C. 78o(b), or with respect to which the company files, or is required to file, periodic information, documents, and reports under subsection (d), 15 U.S.C. 78o(d).

(bb) In the fiscal year ending immediately before the fiscal year in which the services of the Merger and Acquisition Broker are initially engaged with respect to the securities transaction, the company meets either or both of the following conditions (determined in accordance with the historical financial accounting records of the company):

(AA) The earnings of the company before interest, taxes, depreciation, and amortization are less than $25,000,000.

(BB) The gross revenues of the company are less than $250,000,000.

(iii) Merger and Acquisition Broker – The term "Merger and Acquisition Broker" means any broker and any person associated with a broker engaged in the business of effecting securities transactions solely in connection with the transfer of ownership of an eligible privately held company, regardless of whether that broker acts on behalf of a seller or buyer, 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 that –

(I) upon consummation of the transaction, any person acquiring securities or assets of the eligible privately held company, acting alone or in concert, will control and, directly or indirectly, will be active in the management of the eligible privately held company or the business conducted with the assets of the eligible privately held company; and

(II) if any person is offered securities in exchange for securities or assets of the eligible privately held company, such person will, prior to becoming legally bound to consummate the transaction, receive or have reasonable access to the most recent fiscal year-end financial statements of the issuer of the securities as customarily prepared by its management in the normal course of operations and, if the financial statements of the issuer are audited, reviewed, or compiled, any related statement by the independent accountant; a balance sheet dated not more than 120 days before the date of the exchange offer; and information pertaining to the management, business, results of operations for the period covered by the foregoing financial statements, and any material loss contingencies of the issuer.

(iv) PUBLIC SHELL COMPANY – The term "public shell company" is a company that at the time of a transaction with an eligible privately held company –

(1) has any class of securities registered, or required to be registered, with the United States Securities and Exchange Commission under Section 12, 15 U.S.C. 78o(b), or with respect to which the company files, or is required to file, periodic information, documents, and reports under subsection (d), 15 U.S.C. 78o(d); and

(2) has no or nominal operations; and

(3) has –

(aa) no or nominal assets;

(bb) assets consisting solely of cash and cash equivalents; or

(cc) assets consisting of any amount of cash and cash equivalents and nominal other assets.

(F) INFLATION ADJUSTMENT

(i) IN GENERAL – On the date that is five years after the date of the enactment of the rule, and every five years thereafter, each dollar amount in subparagraph (D)(ii)(II) shall be adjusted by –

(1) dividing the annual value of the Employment Cost Index For Wages and Salaries, Private Industry Workers (or any successor index), as published by the Bureau of Labor Statistics, for the calendar year preceding the calendar year in which the adjustment is being made by the annual value of such index (or successor) for the calendar year ending December 31, 2012; and

(11) multiplying such dollar amount by the quotient obtained under sub clause (1).

(ii) ROUNDING – Each dollar amount determined under clause (i) shall be rounded to the nearest multiple of $100,000.

Second Request for Comments

The Broker Dealer Section is interested in receiving comments related to the following questions.

1. A commenter has suggested that the Proposed Rule should be clearer in its prohibition of a Merger and Acquisition Broker facilitating a capital raise for an issuer through a Rule 506(c) offering which is independent from an M&A Transaction. NASAA intends for the Proposed Rule to prohibit a Merger and Acquisition Broker from participating in an issuer capital raise using a Regulation D, Rule 506 offering for something other than an M&A Transaction. In your opinion, does the Proposed Rule need to be further clarified as to this point? If so, what clarification would be useful?

2. A commenter has raised the issue of whether a Merger and Acquisition Broker would be prohibited under the Proposed Rule from advertising an "eligible privately held company" for sale. Should there be clarification in the Proposed Rule about advertising? Should the Proposed Rule specifically regulate what the advertisement should include, such as a description of the business, its general location, and a price range? Should the Proposed Rule speak to the mode of communication for the advertisement (oral, written, electronic)?
3. Some commenters have suggested that NASAA should remove the size cap restriction for an M&A Transaction from the Proposed Rule? Specifically, should paragraphs (E)(ii)(1)(bb) and (F) be deleted from the Proposed Rule? What would be the risks and benefits of doing so? Should the Proposed Rule include optional language to allow states to limit the size of an M&A Transaction based on local industry standards and needs?
4. Certain commenters have suggested that it may be premature for NASAA to adopt the Proposed Rule at this juncture because there is not federal legislation which has been adopted on this topic. If you believe that it is premature for NASAA to adopt the Proposed Rule at this juncture, what is the basis for your position?
5. By contrast, other commenters have suggested that it is not premature for NASAA to adopt a model rule, but that the Proposed Rule should be more in line with the terms and conditions enumerated by the SEC Letter. Commenters pointed to the fact that the SEC Letter allows for a Merger and Acquisition Broker to advertise a company for sale and to represent both buyer and seller in a transaction. However, the SEC Letter limits a Merger and Acquisition Broker's ability to arrange for financing amongst a group of buyers. The Proposed Rule is silent on all of these issues. If NASAA were to adopt a model rule based on the SEC Letter, what are the risks and benefits of doing so?
6. Commenters suggest that there a need to ensure that a Merger and Acquisition Broker is bound by federal anti-money laundering law specifically. While NASAA believes the Proposed Rule does bind a Merger and Acquisition Broker to all federal and state anti-money laundering laws when facilitating an M&A Transaction, should NASAA include additional language to the Proposed Rule for clarification purposes?