

The Campaign for Clarity

Congress Codifies “M&A Broker” Exemption ~ Clarity Brings New Opportunities

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Mission

Our mission is to create and enable activities to uplift the profession through, but not limited to: INFORMATION • AWARENESS • RESEARCH • OUTREACH • ANALYSIS • EXCHANGE • UNDERSTANDING • COOPERATION • EDUCATION

Objectives

First, develop cooperation, education, and interchange among worldwide peers and with related professions

In addition, advise, educate, and persuade business buyers, sellers, and their advisors about the value and wisdom in employing a professional business broker or intermediary when selling, buying, or transferring ownership of a business.

Moreover, cause development and delivery of education and programs to enhance competencies and success throughout the business brokerage, mergers and acquisitions profession or its clientele.

Also, enable study and research into topics of value to the profession and its markets. Finally, establish perpetual self-funding to enable and sustain BIEF's vision and mission.

Campaign for Clarity's presenters

- **J. Michael Ertel**



- **Shane B. Hansen**



- ❑ This presentation has been provided for educational purposes only. It is not based upon an analysis of actual facts and circumstances and so does not constitute legal advice.**
- ❑ Federal and state securities law and regulation is complex and nuanced. State laws, related rules, and related judicial interpretations vary.**
- ❑ Please consult your own attorney for fact-specific guidance.**

Today's road map . . .

- Congress passed it, so now let's read it!
- Turning to the states, 20 down and 30+ to go
- What about FINRA?
- What's an M&A broker to do?
- Answering Your Questions
- Appendix – the exemption's text – cheers!



PART I

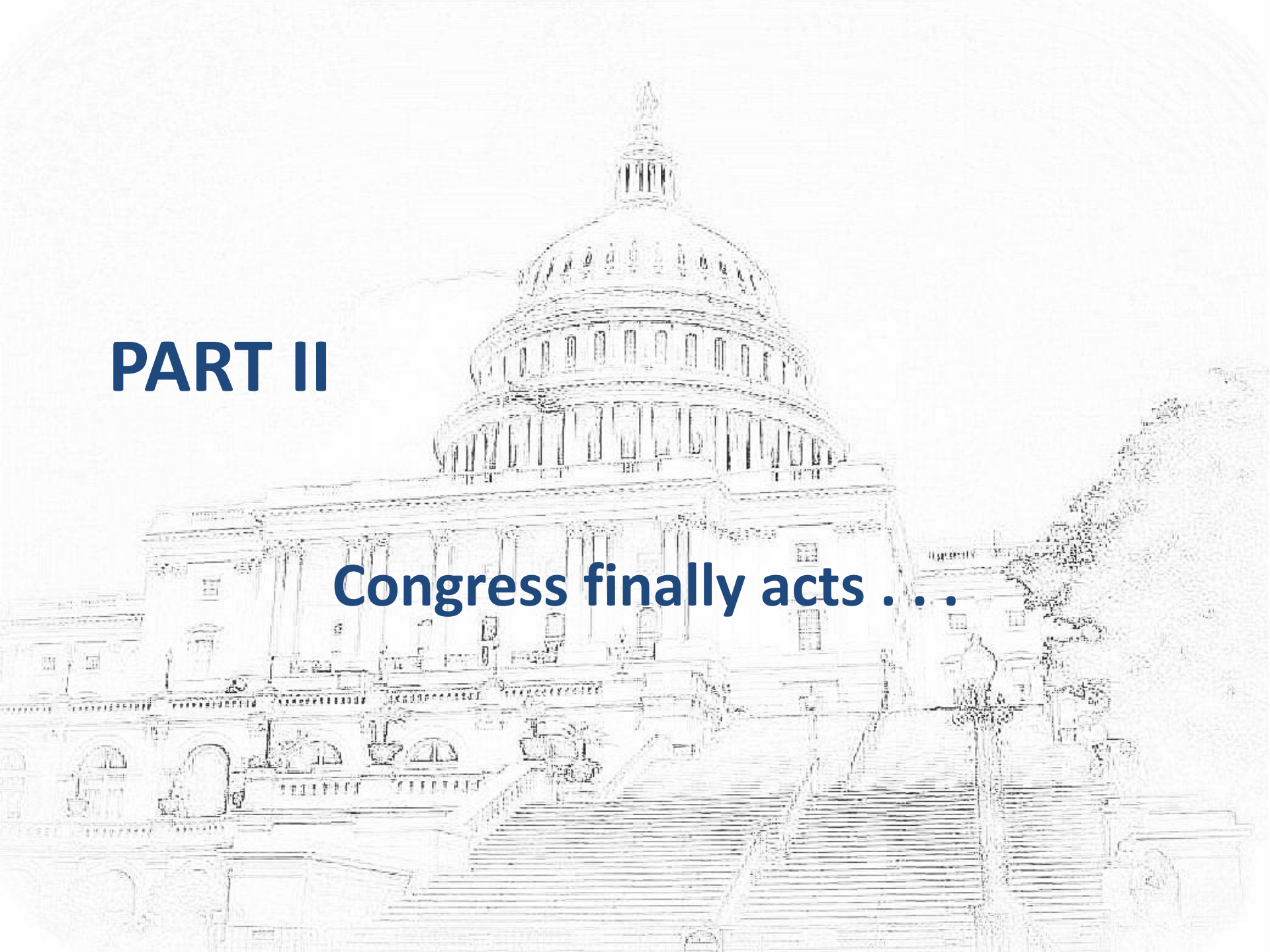
A “brief” history in 16 years or less . . .

How we got here – mile markers

- 2004 – AM&AA considers forming an SEC-registered broker-dealer to support its members
- 2005 – American Bar Association’s Private Placement Broker-Dealer Report and Recommendations
- **2006 – SEC Country Business, Inc. (CBI) No Action Letter**
- 2006 to 2012 SEC M&A broker rulemaking pitch – SEC Small Biz Forum recommendations
- 2013 – 2014 H.R. 2274 M&A broker legislation introduced and **unanimously** passes full U.S. House
- **2014 – SEC staff M&A Brokers no action letter issued to six ABA securities lawyers 2 weeks later**
- 2015 – 2016 H.R. 686 M&A broker legislation reintroduced
- **2015 – North American Securities Administrators Association (NASAA) state model M&AB rule**
- 2017 – 2018 H.R. 477 M&A broker legislation reintroduced and **unanimously** passes full U.S. House
- 2019 – H.R. 609 M&A broker legislation reintroduced – passes full U.S. House as/in three bills
- 2021 – H.R. 935 M&A broker legislation reintroduced and **unanimously** passes full U.S. House
- **2022 – H.R. 2617, Consolidated Appropriations Act, 2023, Division AA, Title V, December 29, 2022**

PART II

Congress finally acts . . .



M&A Brokers Exemption

- Amended Securities and Exchange Act of 1934
 - New registration exemption in Section 15(b)(**13**)
 - Largely codifies the 2014 SEC staff M&AB NAL
 - SEC has withdrawn its M&AB NAL
 - Relevant to some M&ABs because of new size caps
 - Securities laws still apply to securities transactions
 - SEC jurisdiction and all anti-fraud prohibitions
 - State-level B-D exemptions in 20 states
 - Other registration exemptions may be available

M&A Brokers Exemption

- What's affected by the new exemption?
 - Registration as or with a broker-dealer (B-D)
 - Private M&A transactions involving securities
 - Regardless of that deal's ultimate structure
 - "Stock sales" – sale or exchange of securities
 - "Cash-for-assets" sales involving securities
 - Changes federal law only – no change in state laws
 - State real estate and biz broker licensing laws continue
 - Carefully consider state requirements and exemptions

M&A Brokers Exemption

- Scope – private company M&A transactions
 - Target - “eligible privately held company”
 - No SEC-registered securities
 - No “pink sheets” public companies
 - New 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 engagement
 - Metrics apply to target’s actual financial statements
 - Must be an operating company but not a “shell company”
 - Triangular subsidiary mergers are OK, but
 - No “special purpose acquisition company” (SPACs)

M&A Brokers Exemption

- M&A broker must “reasonably believe” 3 things –
 - Buyer will hold a controlling interest; AND
 - Presumption of control at 25% or more
 - Buyer will be active in post-closing management
 - Directly or indirectly – non-exclusive examples (on board, an executive officer, approval of company’s budget)
 - If seller is offered buyer’s securities (e.g., equity rollovers)
 - Buyer must provide seller at/prior to offer of its securities
 - Buyer must provide a current (w/in 120 days) balance sheet
 - Buyer’s last FY financial statements
 - Buyer must provide an MD&A of FY performance
 - Buyer must disclose material loss contingencies

M&A Brokers Exemption

- Conditions to the exemption – M&AB don'ts
 - Cannot have custody, possession or control of \$\$\$
 - Use third-party escrow services for earnest money
 - Reminder – only applies in M&A securities transactions
 - Cannot be engaged by issuer in a public securities offering
 - A public company can be a buyer
 - Cannot directly/indirectly provide deal financing
 - PE/VC firms funding their own fund's deals cannot rely on it
 - Cannot form or facilitate forming group of buyers
 - SEC concerns with creating a private fund of passive buyers
 - SEC concerns with perceived PE firm/fund abuses
 - Cannot be involved in a sale to passive buyers
 - Cannot have a power of attorney to bind a party

M&A Brokers Exemption

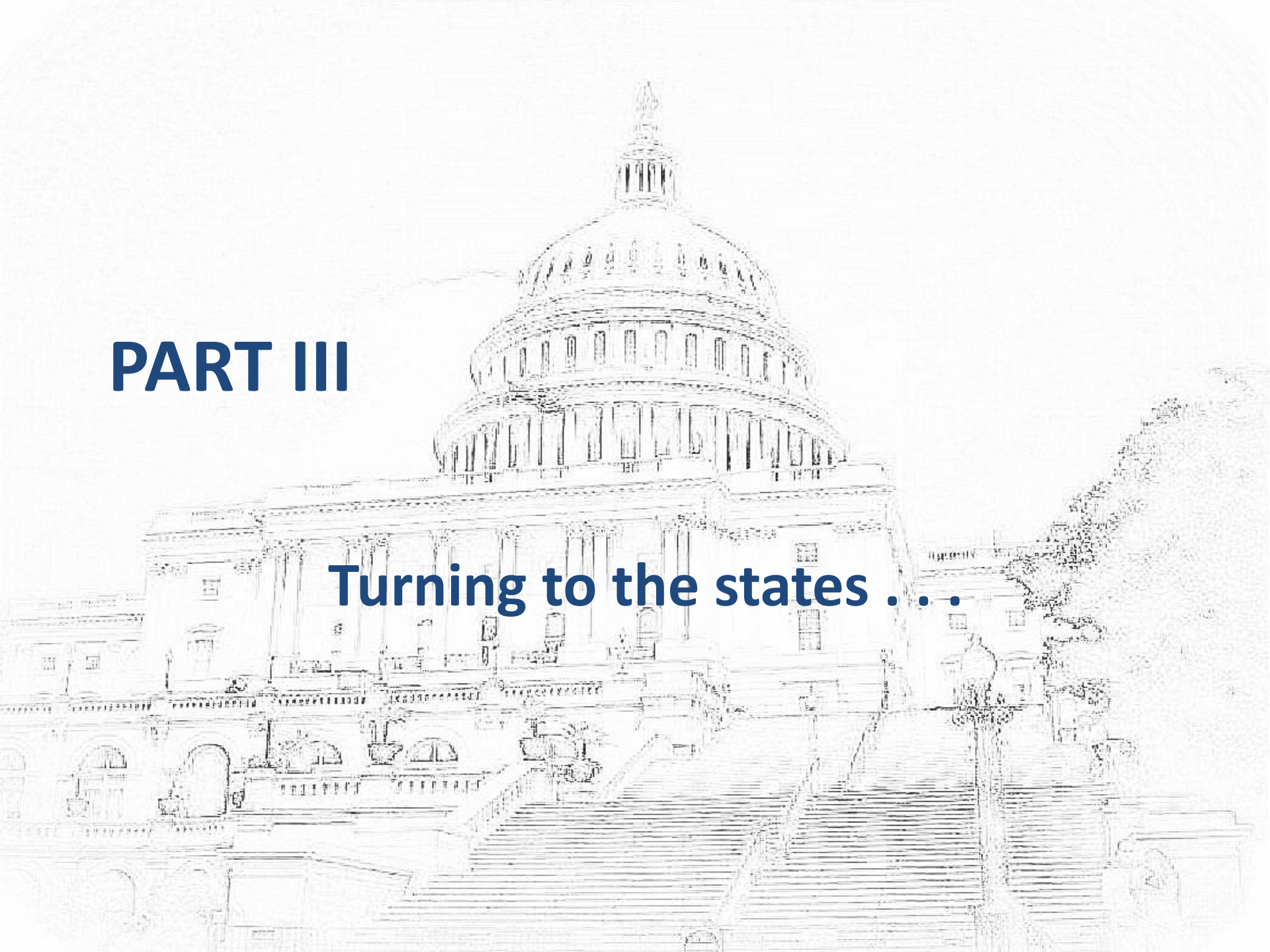
- Permissible activities – M&AB can do's
 - Can be engaged by either seller or buyer
 - Can be a “neutral” broker with disclosure/consent
 - Can assist with obtaining third-party financing
 - Disclosure of role and relationships (and conflicts)
 - Disclosure of any related compensation
 - Does not cover capital-raising
 - M&A Broker's comp is not limited
 - E.g., can be a combination of cash and equity interests
 - No prescribed recordkeeping requirements
 - But think defensively – proving conditions were satisfied

M&A Brokers Exemption

- Disqualifications – M&AB can not's
 - M&A brokerage firm, owners, and management –
 - Cannot be barred from the securities industry
 - Cannot be suspended from securities registration
 - Some state-level exemptions could include additional disqualification types (e.g., state licensing violations)

PART III

Turning to the states . . .



20 States adopted M&A-specific relief

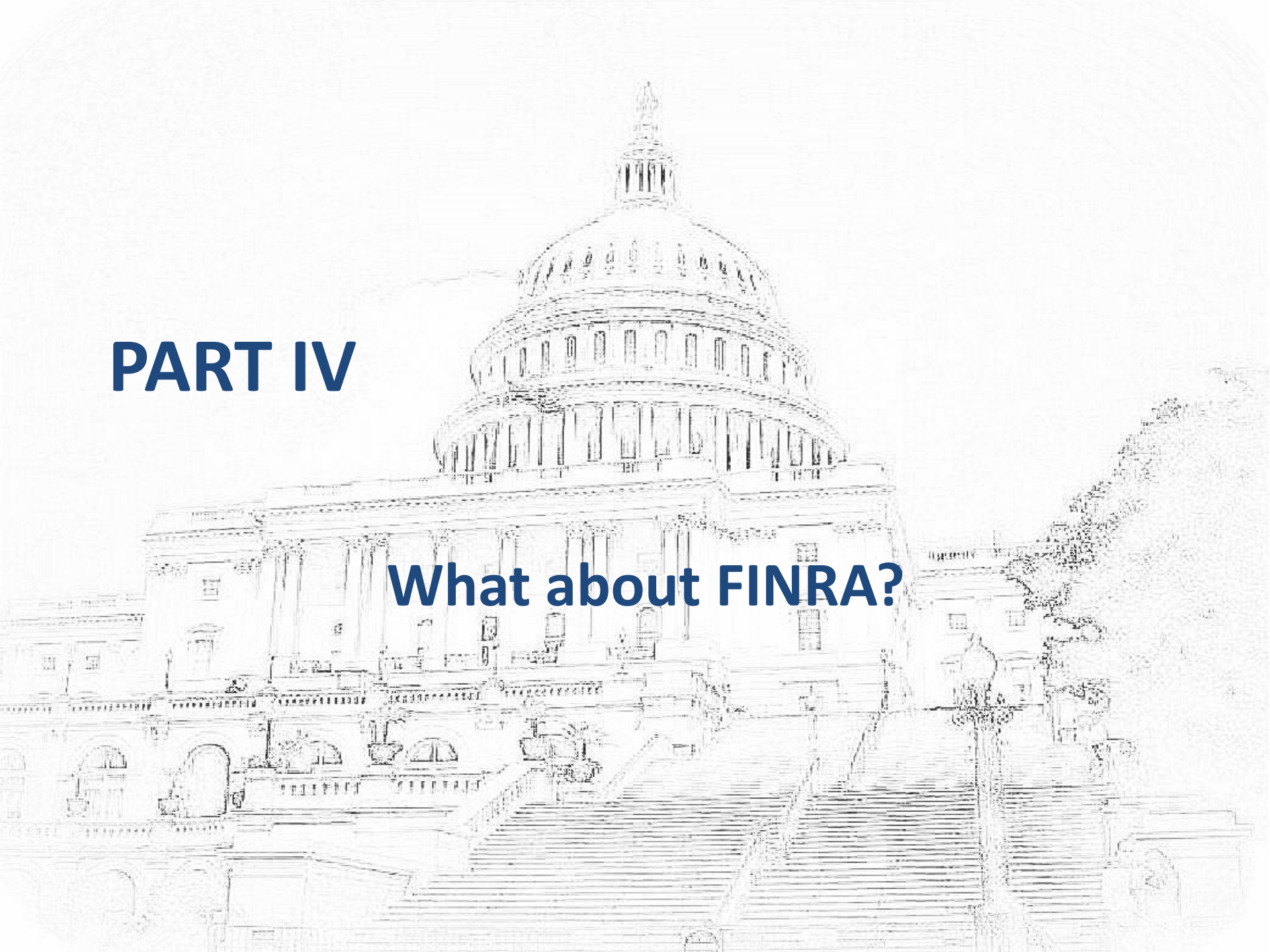
1. Alaska Sec. 45.56.420 Registration Exemption for Merger and Acquisition Broker (2019-01-22)
2. Arkansas Rule 302.01, Merger Acquisition Broker Exemption (2020-10-05)
3. Colorado Rule 51-3.33 Licensing Exemption for Merger and Acquisition Brokers (2017-07-15)
4. Florida Section 517.12(22)(a) Merger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

Just 30⁺ more states and D.C. to go

- North American Securities Administrators Association (NASAA) 2015 model state M&AB rule exemption
<https://www.nasaa.org/wp-content/uploads/2011/07/MA-Broker-Model-Rule-adopted-Sept-29-2015-corrected.pdf>
- **State and regional associations** are key players
 - Contact your state regulator (<https://www.nasaa.org/contact-your-regulator/>) to harmonize theirs with the new exemption
 - Contact your **state's governor**
 - Contact your **state's economic development agency**
 - Contact your **state's legislators**
- Like Florida, some states will likely need lawmaking (e.g., MA, OH, VA) rather than rulemaking

PART IV

What about FINRA?



FINRA Regulation *(of its members)*

- SEC-registered B-Ds must be an “SRO” member
 - SRO = a “self-regulatory organization”
 - Financial Industry Regulatory Authority (FINRA) is the default SRO if B-D is not a stock exchange member
 - FINRA’s jurisdiction and regulation only applies to its members and their FINRA-registered professionals
- SEC/FINRA registration still required for -
 - Securities deals outside scope of M&AB exemption
 - Public offerings of SEC-registered stock/securities
 - Capital-raising from passive investors
 - Fairness opinions, among other securities activities

FINRA Regulation *(of its members)*

- FINRA rules still apply if FINRA-registered, 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 exemption creates a permissible exception
 - 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 – potential liabilities



PART V

What's an M&A broker to do?

What's an M&A broker to do?

- Unregistered M&AB firms and professionals –
 - Review state-level exemptions in multi-state deals
 - Expand M&A-related services with success fees
 - Update your engagement letters –
 - Add “*reasonable belief*” M&AB exemption conditions
 - Cite the new statutory exemption, not SEC M&AB NAL
 - Retain deal dox supporting your “reasonable belief”
 - Update advertising/website disclosures
 - New referral relationships with CPAs, biz valuation appraisers, attorneys, “up-market”, etc.

What's an M&A broker to do?

- FINRA-registered professionals
 - Registration is still required for –
 - Capital raising and related compensated referrals
 - Public and “pink sheet” (thinly traded) companies
 - Fairness opinions
 - All securities transactions outside of the M&AB exemption’s scope
 - If only qualifying private company M&A, then –
 - Still state-level registration uncertainties in 30+ states
 - Consider terminating your FINRA registration, but bear in mind;
 - FINRA B-Ds remain resistant and misunderstand FINRA Rule 2040
 - All FINRA and state exam qualifications will lapse at the 2 year-mark
 - Registration termination by filing Form U5 through the B-D
 - Check termination-related provisions in your B-D rep agreement

What's an M&A broker to do?

- SEC-registered B-D/FINRA member firms –
 - Move M&A practices into unregistered affiliates
 - Still some state-level exemption uncertainties (30+ states)
 - Restructuring could require FINRA approval (it's been done)
 - Compensated referrals – “upstream and downstream”
 - What's the on-going use and value of B-D registration?
 - Capital-raising and fairness opinion engagements
 - M&A securities deals above the exemption's two size caps
 - Public offerings and/or SEC-registered securities
 - Compensated refers for capital-raising and public deals



PART VI

Credits, kudos, and thanks . . .

Supporting Organizations (partial list)

- Alliance of Merger & Acquisition Advisors (AM&AA)
- Association for Corporate Growth (ACG)
- Business Intermediaries Education Fund (BIEF)
- Institute of Certified Business Counselors (ICBC)
- International Business Brokers Association (IBBA)
- International Mergers and Acquisitions Partnership (IMAP)
- M&A Source (MAS)
- Mid Market Alliance (MMA)
- Small Business & Entrepreneurship Council (SBEC)
- Small Business Investor Alliance (SBIA)
- National Association of Media Brokers (NAMB)
- North American Securities Administrators Association (NASAA)
- US Chamber of Commerce

Supporting M&A Associations (partial list)

- Midwest Business Brokers & Intermediaries (MBBI)
- Business Brokers of Florida (BBF)
- Colorado Association of Business Intermediaries (CABI)
- Mid Atlantic Business Intermediaries Association (MABIA)
- Texas Association of Business Brokers (TABB)
- California Association of Business Brokers (CABB)
- Arizona Business Brokers Association (AZBBA)
- Georgia Association of Business Brokers (GABB)
- Michigan Business Brokers Association (MBBA)
- Nevada Business Brokers Association (NBBA)
- Carolinas Virginia Business Brokers Association (CVBBA)
- Ohio Business Brokers Association (OBBA)
- New England Business Brokers Association (NEBBA)
- Pennsylvania Business Brokers Association (PBBA)

PART VII

But before we go . . .



What Else Should I Do TODAY?

- Choose your level of support and contribute on-line, write a check, or make a pledge for your fair share TODAY
 - 2% Sponsor – 2% of Gross Success Fees*
 - 50% Sponsor – 50% of Out-of-Pocket Expense Savings*
 - Angel Investor - \$50,000+*
 - Diamond Sponsor – \$25,000+*
 - Platinum Sponsor – \$15,000+*
 - Gold Sponsor – \$10,000+*
 - Silver Sponsor – \$5,000+*
 - Bronze Sponsor – \$2,500+*
 - Supporter – \$1,000+*

BIEF Campaign for Clarity - Contribution/Pledge Card

- Contribute on-line: <https://www.biefoundation.org/contribute-bief/>
- Contribute by card/pledge (print and mail-in this page):

"Campaign for Clarity"

Yes, I want to contribute my fair share to support BIEF

Suggested Contribution Levels (Please check one)

- Angel Investor – \$50,000
- Diamond – \$25,000
- Platinum – \$15,000
- Gold – \$10,000
- Silver – \$5,000
- Bronze – \$2,500
- Supporter – \$1,000
- Contributor – Under \$1000
- Other – \$ _____
- Please accept my pledge for \$ _____ to be paid on or before December 31, 2023.
- Please accept my pledge for \$ _____ to be paid from my proceeds of my next closing.

My company or association will match my contribution: ___ Yes

Name of Company or Association: _____



PREFERRED PAYMENT OPTIONS

- Contribute directly at www.biefoundation.org
- Check: Payable to Business Intermediary Education Foundation

Credit Card: ___ Visa ___ Mastercard ___ AMEX

Account #: _____

Exp. Date: _____ Sec. Code: _____

NAME: _____

Company: _____

Address: _____

City: _____ State: _____ Zip: _____

Phone: _____

Email: _____

Signature: _____

Mail completed card, along with your check or CC info to:

Campaign for Clarity
c/o Business Intermediary Education Foundation
c/o IBG Business
4643 S Ulster Street, Suite 1295
Denver, CO 80237

Contact Information

- Questions about how to contribute financially, or with your time and resources, contact:
 - Mike Ertel (888) 864-6610,
mertel@transworldma.com
 - John Zayac, (303-758-4000)
zayac@ibgbusiness.com
 - Todd Cushing, (847) 566-0500, +201
tcushing@ebitassociates.com

Other Resources

For more detailed information and latest updates visit these websites:

- **Donate on-line directly at:**
 - <https://www.biefoundation.org/contribute-bief/>
- **Regulatory updates at:**
 - <http://www.biefoundation.org>
 - <https://www.ibba.org/resource-center/legal-updates/>
 - <https://amaaonline.com/campaign-for-clarity/>
 - <https://masource.org/resources/legal-updates/>



PART VIII

Your questions . . .



Appendix

The exemption . . . cheers!

(13) REGISTRATION EXEMPTION FOR MERGER AND ACQUISITION BROKERS.

(A) IN GENERAL. Except as provided in subparagraph (B), an M&A broker shall be exempt from registration under this section.

(B) EXCLUDED ACTIVITIES. An M&A 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 Commission under section 12 or with respect to which the issuer files, or is required to file, periodic information, documents, and reports under subsection (d).

(iii) Engages on behalf of any party in a transaction involving a shell company, other than a business combination related shell company.

(iv) Directly, or indirectly through any of its affiliates, provides financing related to the transfer of ownership of an eligible privately held company.

(v) Assists any party to obtain financing from an unaffiliated third party without —

(I) complying with all other applicable laws in connection with such assistance, including, if applicable, Regulation T (12 C.F.R. 220 et seq.); and

(II) disclosing any compensation in writing to the party.

(vi) Represents both the buyer and the seller in the same transaction without providing clear written disclosure as to the parties the broker represents and obtaining written consent from both parties to the joint representation.

(vii) Facilitates a transaction with a group of buyers formed with the assistance of the M&A broker to acquire the eligible privately held company.

(viii) Engages in a transaction involving the transfer of ownership of an eligible privately held company to a passive buyer or group of passive buyers.

(ix) Binds a party to a transfer of ownership of an eligible privately held company.

(C) **DISQUALIFICATION.** An M&A broker is not exempt from registration under this paragraph if such broker (and if and as applicable, including any officer, director, member, manager, partner, or employee of such broker) —

(i) has been barred from association with a broker or dealer by the Commission, any State, or any self-regulatory organization; or

(ii) is suspended from association with a broker or dealer.

(D) **RULE OF CONSTRUCTION.** Nothing in this paragraph shall be construed to limit any other authority of the Commission 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) **BUSINESS COMBINATION RE-LATED SHELL COMPANY.** The term ‘business combination related shell company’ means a shell company that is formed by an entity that is not a shell company —

(I) solely for the purpose of changing the corporate domicile of that entity solely within the United States; or

(II) solely for the purpose of completing a business combination transaction (as defined under section 230.165(f) of title 17, Code of Federal Regulations) among one or more entities other than the company itself, none of which is a shell company.

(ii) **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 if, upon completion of a transaction, the buyer or group of buyers —

(I) has the right to vote 25 percent or more of a class of voting securities or the power to sell or direct the sale of 25 percent or more of a class of voting securities; or

(II) in the case of a partnership or limited liability company, has the right to receive upon dissolution, or has contributed, 25 percent or more of the capital.

(iii) **ELIGIBLE PRIVATELY HELD COMPANY.** The term 'eligible privately held company' means a privately held company that meets both of the following conditions:

(I) The company does not have any class of securities registered, or required to be registered, with the Commission under section 12 or with respect to which the company files, or is required to file, periodic information, documents, and reports under subsection (d).

(II) In the fiscal year ending immediately before the fiscal year in which the services of the M&A 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.

For purposes of this subclause, the Commission may by rule modify the dollar figures if the Commission determines that such a modification is necessary or appropriate in the public interest or for the protection of investors.

(iv) **M&A BROKER.** The term 'M&A broker' means a 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 the 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 —

(aa) will control the eligible privately held company or the business conducted with the assets of the eligible privately held company; and

(bb) 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, including without limitation, for example, by

- (AA) electing executive officers;
- (BB) approving the annual budget;
- (CC) serving as an executive or other executive manager; or

(DD) carrying out such other activities as the Commission may, by rule, determine to be in the public interest; 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 the management of the issuer 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 offer, and information pertaining to the management, business, results of operations for the period covered by the foregoing financial statements, and material loss contingencies of the issuer.

(v) SHELL COMPANY. The term 'shell company' means a company that at the time of a transaction with an eligible privately held company —

- (I) has no or nominal operations; and
- (II) 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 5 years after the date of the enactment of this paragraph, and every 5 years thereafter, each dollar amount in subparagraph (E)(iii)(II) shall be adjusted by —

(I) 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, 2020; and

(II) multiplying such dollar amount by the quotient obtained under subclause (I).

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