SECURITAS
FINANCIAL LAW

November 12, 2020

U.S. Securities and Exchange Commission
Attn: Vanessa A. Countryman, Secretary
100 F. Street NE
Washington, DC 20549-1090

VIA EMAIL ONLY:
rule-comments@sec.gov

RE: Securities and Exchange Commission ("SEC"), *Notice of Proposed Exemptive Order Granting Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Finders*, 85 Fed. Reg. 64,542, File No. S7-13-20, Oct. 13, 2020 (the "*Release*")

Dear Ms. Countryman,

I am an attorney in private practice representing a variety of clients active in the capital markets and merger and acquisition ("M&A") space. These clients include companies seeking capital, acquisitions, or mergers; individual investors; finders; broker-dealers; and investment advisers. I am also a former Kansas Securities Commissioner and therefore comment with an eye toward fulfillment of the purposes of securities regulation, namely, the protection of small investors.

Though I provide specifics below, my conclusion is that the SEC should adopt the proposed exemption inclusive of the very same M&A brokers to which it directed the *M&A Broker* No-Action Letter,[1] and to the same extent as set forth in the letter. As proposed, the finder exemption will benefit only highly risky early-stage startups making initial offerings. This benefits only a very small universe of businesses utilizing a very narrow type of transaction that may not even be appropriate for its capital needs. From an investor protection perspective, it results in the riskiest transactions being placed before investors, riskier than the alternatives discussed below.

I. There is an Investment Capital and Expertise Gap that Must be Filled

I agree with the stated purpose of the *Release*. As noted, small businesses have issues raising capital. They certainly have trouble accessing the services of registered broker-dealers, those who are in the best position to identify accredited investors – always consistent with their duties to clients – with the ability and desire to invest in private offerings. The universe of accredited investors in any given region who are also knowledgeable about an issuer's line of business and comfortable with early stage investment is infinitesimal. Registered broker-dealers

[1] *M&A Brokers*, SEC Staff No-Action Letter (Jan. 31, 2014) ("*M&A Broker* Letter"). This framework also includes the other no-action letters cited in *Release*, n.51, *16.

generally won't touch small businesses, not because individual registered representatives are not so inclined, but because FINRA places upon registrants a very high burden of due diligence and disclosure, one that may not be affordable or appropriate for a small issuer.[2]

Therefore, there is an investment capital gap that needs to be filled, a need for small businesses to interact with networks of accredited investors to which they would not otherwise have access. Especially because registered broker-dealers are not fulfilling that role, finders should be able to do so with a clear exemption from registration, and not merely in reliance upon no-action letters.[3] Finders need legal certainty in order to represent to their clients that they are not required to be registered, as well as to enforce their contractual rights. Likewise, counterparties deserve to know where finders stand legally lest they risk utilizing an unregistered broker-dealer and suffering the attendant consequences.[4] All sides of any transaction – investor, issuer or finder – need to know explicitly where finders cross the line into activity for which they are required to be registered.

II. The SEC Implements the M&A Broker Framework – but not for M&A Brokers?

The SEC's proposal in the *Release* seems unnecessarily narrow in that it only serves the needs of (i) risky early-stage startups that are (ii) raising capital from multiple individual investors in only (iii) a primary offering.[5] This singular model seems to serve only startups at an early stage, not the full range of small businesses that should benefit from this exemption, whatever their stage or need. To serve the full range of small businesses, there are other appropriate transactional models for raising or restructuring capital that may be more appropriate. These transactions should, and can easily be, covered by the proposed finder exemption, including strategic mergers or acquisitions, divestitures, joint ventures, leveraged buyouts, recapitalizations, consolidations, reorganizations, restructuring, or other kinds of business combinations.

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[2] Most registered broker-dealers are built to transact in the highly-regulated retail capital markets, not to conduct one-off due diligence investigations of small issuers. Those who are capable of doing so are often not inclined because of the cost, the perceived lack of return on investment, and the increased legal risk of participation in exempt private offerings. Those registered broker-dealers desiring to cater to small issuers and early-stage businesses receive heightened scrutiny from FINRA, sometimes to the point that they feel "regulated out of existence." I had one client focused primarily on private offerings that chose to surrender FINRA licensure for that very reason.

[3] My clients who want to merely introduce potential transaction partners are incredulous when I inform them that they may be subject to FINRA registration, that the SEC has not made a clear exemption for finders, and that few state regulators have done so, either. Those who engage in finder activities find it difficult to explain to clients their limited role, and to counterparties why they do not need to be registered. Providing a client or counterparty a regulation and proof of compliance is much better than providing a copy of a no-action letter upon which the parties may not be able to rely.

[4] *E.g.*, rescission rights, civil and criminal penalties, accounting issues, inability to utilize private offering exemptions or conduct an initial public offering, *etc*.

[5] *See*, *Release*, **28-29 (finders may only facilitate "…activities solely in connection with primary offerings…," and may not facilitate "…a resale of securities…"). I note that these investments are highly risky, especially compared to a small business with an operating history that made previous offerings. I can see no reason why a finder exemption should not benefit small businesses like these and the investors who want to make a safer investment choice.

The *M&A Broker* Letter[6] covers these forms of capital structuring that many small businesses should consider, but the *Release* contemplates only the narrow model of the riskiest offerings. Clearly, the SEC is proposing to implement the framework of the *M&A Broker* Letter for Tier II finders, but as drafted, the Tier II exemption fails to include the very M&A brokers for which the SEC developed the guidance in the first place. Failure to include in the proposed exemption the M&A brokers who currently rely on the *M&A Broker* Letter and is forebears is a *huge* missed opportunity not only for small businesses, but for the economy as a whole.

The types of transactions the proposed finder exemption apparently will *not* apply to include transactions that are perfectly appropriate for finders. Examples of capital transactions that I have personally seen in my practice include (i) sales of securities in family business owned by an older generation to a new strategic merger or acquisition partner, or a management team, better positioned to grow the business; (ii) the sale of subsidiary operations of a small business so that the business may utilize the capital to grow its core lines; (iii) an exchange of equity in a small business for equity in a strategic partner that will benefit equityholders of both companies; (iv) new offerings of securities of a closely-held company to persons with experience in the industry and who participate in governance to provide the benefit of that experience; and (v) private funds that wish to mitigate and spread risk in in a deal by bringing in other investors, or because the deal is too large for them to handle on their own. I have also seen finders identifying transaction partners for the purchase, transfer or exchange of reinsurance risk[7] on behalf of companies that are large, sophisticated, and highly-regulated, precisely the kind of market players the securities laws were *not* designed to protect.[8] Because these types of transactions do not involve small investors, the need for regulatory oversight of these types of transactions is reduced, making a finder exemption that follows the *M&A Broker* Letter a very useful exemption for small business capital formation.

These deals did not involve companies that are registered with or must report to the SEC, nor were they effected pursuant to a specific exemption in securities laws,[9] like Regulation D, because securities laws were simply not implicated on account of the types of parties and deal structure.[10] These types of deals almost certainly raise and inject more capital into small businesses every year than initial offerings by startups. Therefore, if the purpose of the finder exemption is to serve the needs of small businesses, it should be crafted more broadly to serve the needs of businesses other than startups. It needs to also serve proven and profitable small businesses that have been around many years, and those at varying stages of their business lifecycle. The *M&A Broker* Letter provides a role for finders in the above types of transactions, but the proposed exemption apparently does not embrace and provide the certainty and stability M&A brokers deserve given their outsized role in growth of the economy, job creation, and providing value for equityholders.

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[6] *M&A Brokers*, SEC Staff No-Action Letter (Jan. 31, 2014) ("*M&A Broker* Letter"). This framework also includes the other no-action letters cited in *Release*, n.51, *16.

[7] Like many transactions in which finders may be involved, these deals start out as potential asset purchases or sales, and the parties later decide, independently of the finder and with the benefit of their legal and accounting counsel, to effect the transaction in securities rather than assets. The *M&A Broker* Letter contemplates finders being compensated for these types of transactions, but the *Release* seems to rule them out.

[8] This finder was also registered as a "reinsurance intermediary" with state insurance regulators pursuant to state insurance laws and subject to their jurisdiction.

[9] *Release*, *18 (second bullet point).

[10] Obviously, the anti-fraud provisions of the securities laws apply.

In sum, however the proposed finder exemption is eventually adopted, it should include those for whom the framework was initially intended. Supposedly, the *M&A Broker* Letter framework would still be available to M&A brokers if the proposed exemption did not specifically include them, but the proposed exemption – including the disclosure requirements – would provide the legal certainty, clarity, and stability small businesses and finders do not currently enjoy from a series of no-action letters. Further, a federal finder exemption provides a clear path for state regulators to follow when either recognizing the federal exemption or crafting their own.

III. Specific SEC Questions

3. Should the definition of Finder be limited to natural persons?

Absolutely not. Finders are small businesses, too, just like the clients they serve. There is no reason why a finder should be denied the basic personal liability protections available to any other small business owners, especially when the anti-fraud securities laws could personally reach the owners or managers of a corporate finder under the right factual circumstances.

5. Have we appropriately identified the activities in which each tier of Finder should and should not be able to engage? Does the proposed exemption provide a workable path for Finders to be engaged in this activity?

As set forth above, if the purpose is to benefit all small businesses (as opposed only to initial private offerings by early stage startups), then the exemption should expressly include M&A brokers as set forth in the *M&A Broker* Letter and its forebears. As drafted, the exemption addresses only the riskiest investments – initial private offerings of early-stage startups. If the exemption followed the *M&A Broker* Letter, investors would have a much greater universe of less risky transactions in which to invest, including in small businesses with lengthy operational track records.

6. Have we appropriately limited the types of investors whom a Finder can "find" or solicit? Instead of limiting potential investors to those the Finder reasonably believes are accredited investors, should investors identified by Finders be subject to investment limitations, regardless of the exemption being relied upon, such as a dollar limit on the size of the investment? If so, please specify.

Finders should not be soliciting small investors; therefore, it is appropriate that any person or entity solicited fit the definition of "accredited investor" as defined in Regulation D. However, regarding the examples above of transactions and transaction partners of various sizes and sophistication, investment size limitations would be antithetical to the purpose of aiding small businesses raise capital in the variety of ways it is appropriate for them to do so. A finder should not be denied a fee for their service on account of deal size.

8. Should we limit the proposed exemption to offerings of a specific size threshold? If so, how should we define such threshold?

No, for the reasons stated in Question 6, above.

9. Have we appropriately limited the number of offerings a Tier I Finder can participate in on an annual basis?

No. The SEC is adopting the *M&A Broker* Letter framework for Tier II finders, and adopting the *Paul Anka* Letter framework for Tier I finders. As proposed, though, the Tier I exemption does not permit the full latitude of the previous guidance; the SEC did not place time restrictions on Mr. Anka in the *Paul Anka* Letter. Logically, if someone like Paul Anka wanted to serve as a Tier I finder several times a year, *i.e., simply make introductions*, it would present no additional risk to non-accredited investors, and it would certainly help small businesses. Perhaps a *de minimis* standard should be utilized here, maybe three or five transactions a year, just as most states use for isolated transactions of broker-dealers.

10. Is the limitation that Tier I Finders do not have any contact with potential investors about the issuer workable? Should we instead permit Tier I Finders to have some contact with potential investors?

No, it is not workable. It is appropriate for a Tier I finder to notify the potential investor they have been referred to a potential transaction partner by the finder and why. Discussion with the potential investor of the who, what, when, where, why, and how of the finder's relationship with an issuer is appropriate. Hopefully, this type of contact is permitted along with the required disclosures. Certainly, discussion of the same regarding the merits or advisability of the deal itself should be prohibited in a finder / investor relationship.

11. Should we define "capital raising transaction" for purposes of Tier 1? If so, how?

If defined, it should include the multitude of other types of transactions that benefit small businesses, as set forth in <u>Section II</u>, above and as set forth in the *M&A Broker* Letter. The proposed exemption is unnecessarily narrow in that it is limited to risky, early-stage initial private offerings.

12. Have we appropriately defined the conditions that should apply to the proposed exemption for each tier of Finder? Is more clarity, specificity or flexibility required with respect to the proposed conditions? Are there other or different conditions that should apply to the proposed exemption?

As set forth in <u>Section II</u> above, some transactions do not implicate the securities laws to a great degree because they occur between and among sophisticated private parties the securities laws are not designed to protect. Query whether a finder engages in prohibited "structuring" of the transaction by insisting that a client utilize a specific exemption. Adoption of the *M&A Broker* Letter standards provides the necessary clarity, along with flexibility for the parties.

13. Should Finders be able to "find" or solicit investors only for exempt offerings, as proposed? Should Finders be able to "find" or solicit investors only for offerings under certain exemptions from registration? If so, which ones?

No. See response to Question 12, above.

14. Should Finders be able to "find" or solicit for all non-Exchange Act reporting companies or should they be able to solicit for a narrower or wider range of companies?

Yes. Adoption of the *M&A Broker* Letter standards provides a flexible framework, and would also result in a greater diversity of less risky transactions being presented to investors.

15. Should Finders only be able to "find" or solicit for primary offerings? Should we expand the scope of the proposed exemption to secondary offerings, such as transactions facilitating the sale of equity by employees holding options or warrants?

No to limiting the exemption to primary offerings for the reasons sated in <u>Section II</u>, above. Yes to expansion. The exemption should apply to the same extent as those operating under the *M&A Broker* Letter framework.

16. Should the proposed exemption include limitations on the types of securities for which a Finder can "find" or solicit investors?

No. Finders find transaction partners with aligned interests; they do not structure deals. If the parties to a transaction decide independently that a deal should be executed in a certain way, that is outside the purpose and scope of a finder's services. Finders should not be denied a fee because a deal is restructured by attorneys or accountants for the benefit of their client.

17. Is more clarity or specificity required with respect to the specific written disclosures that are a condition of the proposed exemption for Tier II Finders? Should we provide more guidance about any of the specific written disclosures?

Written disclosures are critically important for all parties involved. Disclosures will identify for the parties the precise role of the finder, what they do, what they do not do, and for whose interest they are advocating. Especially if applied to M&A brokers, the disclosures are an easy and sure way for attorneys like me to identify when participants are operating within the law. If a client provided me disclosures sent to them by a finder, and with minimal investigation of the proposed deal terms, I would be able to inform the client that the finder is within the exemption and the finder's compliance reduces risk for all parties. Currently, if I encounter a finder in a deal, I must explain to my client the risks to them and the company in which they are about to invest, and that all are relying on a series of no-action letters, not an actual regulatory exemption.

18. Are there any specific written disclosures to investors that should be required, beyond those that are a condition of the proposed exemption for Tier II Finders? Should the disclosures be required to be written or should the Finder be permitted to provide them orally? Should the written disclosures be required at all?

The disclosures should be in writing not only for the benefit of the investor, but for the protection of the finder, and the ease with which professional advisors can ascertain compliance with the law.

20. Should Tier II Finders be required to receive an acknowledgment of receipt of the required disclosure from the investor? If so, are there methods other than an acknowledgment, for example, a read receipt for e-mail, that could serve to validate that investors received the required disclosure?

Yes. A receipt signed by the investor would be advisable, in the same manner as an investor might fill out a questionnaire certifying they are accredited. There is no reason to rely on oral disclosures; it is an invitation to confusion and litigation.

21. Should Tier I Finders be subject to a disclosure and acknowledgment requirement?

Yes. All parties deserve a clear understanding of the role of a finder in any transaction.

22. Should Tier II Finders be required to enter into a written agreement with the issuer where the issuer, without affecting the Finder's obligations, also assumes liability with respect to investors for the Finder's misstatements in the course of his or her engagement by the issuer?

No. The proposed rule prohibits finders from discussing the merits of the proposed deal with investors, and the anti-fraud securities laws always apply in the right circumstances.

23. Should the proposed exemption be conditioned on a Finder filing a notice with the Commission of reliance on the exemption from registration? Why or why not? If so, when should Finders be required to file the notice? What, if any, disclosures should be required in the notice?

No. There is no regulatory purpose for doing so, and it would create paperwork and compliance expense for both finders and the SEC. If a securities regulator fields a complaint about a finder, they can find out immediately if the finder is in compliance by requesting copies of written agreements and disclosures. Further, finders do not represent systemic risk in the same manner as an exempt reporting advisers might. Securities regulators have better things to do.

24. Should there be any limitations on the amount of fee a Finder can receive?

No, but if there are limits, they should be defined by a reasonableness standard applicable to other securities industry registrants.

25. Should we impose limitations on the form of compensation Finders can receive? Should Finders be prohibited in certain circumstances from receiving transaction-based compensation, and instead be required to receive compensation that is not tied to the success of the transaction (that is a fixed fee or other arrangement)? If so, under what circumstances and how should Finders then be compensated?

No. It is very difficult to predict in advance the value of the finder's services. In the end, transaction-based compensation often accurately reflects that value, whether the finder under- or over-performs.

26. Should a Finder be able to receive a financial interest in an issuer as compensation for its services? Why or why not?

Yes. Part of the purpose of the proposed rule is to fully disclose the interests of the finder and how they are aligned with that of the issuer. Full disclosure would include such an arrangement. It may also inure to the benefit of the investor in that the issuer will not be required to utilize part of the capital raised in the transaction to pay a finder. That capital would instead be directed to the business purposes of the issuer.

27. Are the explicit limitations on the activities in which Finders can or cannot engage appropriate for each tier of Finder? What other activities should be expressly permitted or prohibited for each class of Finder?

If desired by their clients, finders should be able to provide their clients deal analysis and advice on structure. Finders should be able to interact with and provide observations to their clients' professionals engaged in legal, accounting, and due diligence activities. Because many finders formerly worked within the industry in which they advise issuers, M&A finders are often the most experienced voice in the room. They know what questions should be posed and issues raised, and their clients should be able to benefit from their finder's insight. The SEC is correct, however, to prevent finder interaction with counterparties in negotiation. Given their limited role, finders should leave those matters to other professionals. There is no reason, though, that finders should not have these discussions with their own clients.

28. Should we provide guidance on how a Finder can establish that he or she did not know and, in the exercise of reasonable care, could not have known, that the issuer had failed to comply with the conditions of an exemption?

No. A finder is not a legal professional and should not have the burden of making that determination. They should be able to rely on the representations of the issuer, likely made in the finder's written agreement with the issuer, that they are conducting their offering in compliance with the law.

29. Should we provide further guidance on the solicitation-related activities in which Tier II Finders can engage on behalf of an issuer, for example, guidance surrounding a Tier II Finder's discussion of issuer information and arrangement and participation in meetings with issuers and investors?

If that guidance follows the *M&A Broker* Letter, yes. *See, also*, answer to Question 27, above.

30. Should we provide guidance regarding activities of private fund advisers, M&A Brokers as defined in the *M&A Broker* Letter, or real estate brokers that may require registration under Section 15(a) of the Exchange Act? Should we consider codifying the *M&A Broker* Letter?

Yes. These comments strongly urge a regulation following the *M&A Broker* Letter for the reasons stated herein.

31. Are there other areas in which the Commission should provide guidance regarding the registration requirements of Section 15(a) of the Exchange Act to other types of limited-purpose broker-dealers?

It would be helpful for the SEC to provide guidance on finders operating in heavily-regulated industries, like insurance and banking, where they are subject to the oversight of insurance commissioners and federal and state bank regulators.

32. If the proposed exemption is adopted, which staff letters, if any, should or should not be withdrawn, and why?

If the regulation is adopted as proposed, no staff letters should be withdrawn. Doing so would severely impair corporate capital formation for small businesses in the United States. If the rule follows the existing guidance of the *M&A Broker* Letter and its forebears, those letters may be withdrawn. *See, Release*, n.51, *16.

33. Have we appropriately defined the disqualification condition for Finders?

Making finders subject to the same "bad actor" disqualification conditions that apply to issuers and their affiliates will enhance trust in the industry. No M&A broker wants to see those who have been disqualified in other industries move into the M&A broker space because the disqualification conditions do not apply.

35. Should the proposed exemption include a limitation such that it would not be available to individuals who were associated persons of a broker-dealer within the previous 12 months?

I fail to see the utility of this requirement here, or in other places it is utilized, for example, SEC Rule 3a4-1. One is either in the industry or out, and should not be subject to tail regulation or restrictions.

38. Would the proposed exemption provide sufficient investor protections while promoting capital formation for small businesses?

No, for the reasons stated in <u>Section II</u>, above.

39. Would the proposed exemption have a competitive impact on registered brokers?

If adopted as set forth in the *M&A Broker* Letter, it would not have any further impact on registered brokers than they experience from M&A brokers who currently rely on no-action letters

41. Should we instead take an alternative approach for either class of Finders?

Yes. Permit Tier II finders to operate as M&A brokers are permitted to now.

43. Should we coordinate with other regulators to provide clarity and consistency on what types of activities Finders and other limited purpose brokers may engage in?

Absolutely. Conflicting federal and state laws and regulations are the bane of M&A brokers. To the extent state and federal regulation of finders is harmonized, the clarity will benefit small business capital formation.

Thank you for the opportunity to provide comments. Please direct all future correspondence regarding this matter, if any, to me at the letterhead address above.

Very truly yours,

/s/Marc S. Wilson

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