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Submitted via email to: rule-comments@sec.gov

Vanessa Countryman, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: 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 (Release No. 34-90112; File No. S7-13-20)

Dear Ms. Countryman:

This letter is submitted on behalf of the Federal Regulation of Securities Committee (the "Committee") of the Business Law Section (the "Section") of the American Bar Association (the "ABA") in response to the request for comments by the Securities and Exchange Commission (the "SEC") with respect to its proposal to grant exemptive relief (the "Proposed Exemption") to permit natural persons to engage in certain limited securities-related activities on behalf of issuers without such persons (referred to in the Proposed Exemption and this letter as "Finders") being required to register with the Securities and Exchange Commission (the "SEC" or "Commission") as brokers under Section 15(a) of the Securities Exchange Act of 1934 (the "Exchange Act"), as more fully set forth below.[1]

This letter was prepared by members of the Committee's Trading and Markets Subcommittee. The comments expressed in this letter represent the views of the Committee only and have not been approved by the ABA's House of Delegates or Board of Governors, and should not be construed as representing the official policy of the ABA. In addition, this letter does not represent the official position of the Section, nor does it necessarily reflect the views of all members of the Committee.

1 *See* SEC Release No. 34-90112 (October 28, 2020) (the "Release").

The Proposed Exemption provides for two classes of Finders: Tier I Finders and Tier II Finders. All Finders are subject to certain shared conditions and, in addition, Tier I Finders and Tier II Finders are each subject to certain specific conditions tailored to the scope of their respective activities.

Finders whose activities meet the relevant conditions under either tier would be exempt from the requirement to register as a broker under the Exchange Act and would be permitted to receive transaction-based compensation in connection with such activities, so long as the activities engaged in are consistent with those permitted by the relevant tier. The SEC stated in the Release that it believes that the Proposed Exemption "would provide clarity to investors and issuers, and establish clear lanes for both registered broker activity and limited activity by finders that would be exempt from registration."[2] The Committee supports the Proposed Exemption and the SEC's efforts to provide further clarity to this area, but with the changes we recommend below to eliminate some of the conditions that are unnecessary and, in some cases, unrealistic. The Committee believes that the such an exemption would appropriately address the principal issues raised in the 2005 report of the ABA Task Force on Private Placement Broker-Dealers[3] and that it is generally consistent with the goals stated therein. Moreover, we believe the Proposed Exemption will serve as a consistent and logical companion to the no-action letter issued by the SEC staff regarding so-called "M&A Brokers."[4] Finally, we believe that additional clarity in this area is timely, particularly in light of the general focus by the SEC and other regulators in recent years on fostering capital formation opportunities in the U.S. and reducing unnecessary burdens and cost inherent in the capital raising process. As the Release observes, the Commission itself has not broadly addressed whether and under what circumstances a person may "find" or solicit investors on behalf of an issuer without registering as a broker-dealer.[5] The Commission staff has provided no-action relief to "finders" in some situations,[6] while denying relief to others on facts that seem very similar.[7] In any event, no-action letters by their nature only express a view on whether the conduct described would be referred for enforcement consideration, and further only express the views of the Commission Staff, not the full Commission. As Chairman Clayton has emphasized, "all staff statements are nonbinding and create no enforceable legal rights or obligations of the Commission or other parties."[8] Further, only statements of the full Commission,

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2 Release, at p.10.

3 *See* Report and Recommendations of the American Bar Association Business Law Section Task Force on Private Placement Broker-Dealers (June 20, 2005).

4 *See* M&A Brokers, SEC Staff No-Action Letter (Jan. 31, 2014) ("M&A Broker Letter").

5 *See* Release, at p.14.

6 *See* Country Business, Inc. Staff No-Action Letter (Nov. 8, 2006); Paul Anka, SEC Staff No-Action Letter (July 24, 1991), Victoria Bancroft SEC Staff No-Action Letter (July 9, 1987); International Business Exchange Corporation Staff No-Action Letter (Dec. 12, 1986).

7 *See* Brumberg, Mackey & Wall, PLC Staff No-Action Letter (May 17, 2010); John Loofbourrow Associates, Inc. Staff No-Action Letter (June 29, 2006). *See also* Dominion Resources, Inc. Staff No-Action Letter (March 7, 2000); *cf.* Dominion Resources, Inc. Staff No-Action Letter (August 22, 1985).

8 Chairman Jay Clayton, Statement Regarding SEC Staff Views (Sept. 13, 2018).

not its staff, are entitled to judicial deference.[9] As a result, certain federal courts have been reluctant to deem persons engaged in limited finder activity to be "engaged in the business" of effecting securities transactions on facts where the Commission staff might have come to a different result.[10] In short, there is substantial uncertainty under existing law as to whether and when Finders activity rises to the level of "effecting transactions in securities for the account of others," thus triggering a requirement to register under Section 15(a) of the Exchange Act in the absence of any other exclusion or exemption.[11] This lack of clarity has the potential to hinder the Commission's ability to achieve its dual mandates of investor protection through its enforcement program against unscrupulous bad actors and of capital formation for, among others, start-ups and small businesses. The Commission should take this opportunity to clarify this longstanding area of legal uncertainty.

Although the Committee is supportive of the Proposed Exemption, we believe, as discussed below, that certain modifications and clarifications to the Proposed Exemption would enhance the utility of the Proposed Exemption and further the SEC's goals as expressed in the Release.

A. Requirement to Not Provide Advice as to the Valuation or Advisability of the Investment

Although Tier II Finders would be permitted to engage in certain solicitation-related activities including identifying, screening, and contacting potential investors as well as discussing issuer information included in the issuers' offering materials with potential investors, such Finders (as would be the case for Tier I Finders) would not be permitted to "provide advice as to the valuation or financial advisability of the investment."[12] We believe that prohibiting advice as to the financial advisability of an investment is unnecessarily restrictive of Tier II Finders' activities and would create considerable ambiguity as to the parameters of their permitted activities. That is, in the context of introducing a prospective investor to an issuer or approaching a prospective investor to determine the investor's interest in being introduced to the issuer it can be expected that the Finder and prospective investor might discuss the particular investment for which the introduction will be made. Advising on financial advisability sounds a lot like making a recommendation. Because SEC gives a broad reading to the term "recommendation,"[13] a

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9 Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc., 468 U.S. 837 (1984).

10 *See e.g.* SEC v. Kramer, 778 F. Supp. 2d (M.D. Fla. 2011); SEC v. Mapp, No. 4:16-CV-00246, 2017 BL 401498 (E.D. Tex. 2017).

11 For example, the bank networking exception from the "broker" definition in Section 3(a)(4)(B) and the intrastate broker registration exception in Section 15(a)(1) of the Exchange Act.

12 Release, at p.28.

13 *See, e.g.*, SEC Release No. 34-86031 (June 5, 2019) ("Reg BI Adopting Release"), available at https://www.sec.gov/rules/final/2019/34-86031.pdf, at pp. 78-92. In the Reg BI Adopting Release, the SEC stated that factors to be considered in determining whether a recommendation has taken place include whether the communication (i) could reasonably be viewed as a "call to action" and (ii) would reasonably influence an investor to trade a particular security or group of securities. *Id.* at pp.79-80. The SEC also stated "the more individually tailored the communication to a specific customer or a targeted group of customers about a security or group of

suggestion that an investor make – or even simply consider making – an investment decision with respect to a particular investment could be deemed a recommendation, which could be construed as providing advice regarding the "advisability of the investment." Indeed, the mere act of identifying an investment to an investor could be deemed a recommendation. If the limitation with respect to providing "advice as to the valuation or financial advisability of the investment" is to be understood as a limitation on discussing a potential investment, it is unclear how Tier II Finders would be able identify, screen and contact investors and meaningfully discuss issuers' offering materials with them without failing this condition.[14]

Given these ambiguities, the Committee believes that this condition is unduly restrictive and unnecessary to accomplish the Commission's stated goals in light of the other required conditions and parameters of the Proposed Exemption. The Committee also notes that there is no such corresponding restriction in the M&A Broker Letter.

B. Requirement to Not Participate in the Preparation of Sales Materials

The Proposed Exemption would not allow any Finder to participate in the preparation of any sales materials.[15] Similar to the requirement not to provide advice as to the valuation or advisability of an investment discussed above, the Committee believes that this restriction is unnecessarily restrictive as it relates to Tier II Finders and is inconsistent with the solicitation-related activities in which Tier II Finders would otherwise be permitted to engage under the Proposed Exemption. For example, any type of written outreach that a Tier II Finder may make, including an introductory email, could potentially be deemed "sales materials" for this purpose and thus render the exemption unavailable.

The Committee recognizes that the SEC intends to restrict Finders from expanding their activities beyond simple finder activity to activities with respect to which SEC-registered broker-dealers may engage. However, participation in the preparation of "sales materials" is not by itself a recognized broker-dealer activity.[16] Given the difficulty of delineating what may constitute "sales materials" in this context, the Committee suggests either eliminating this restriction or

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securities, the greater the likelihood that the communication may be viewed as a 'recommendation'". *Id.*

[14] The Committee notes that the question of whether the provision of such advice might require registration under the Investment Advisers Act of 1940 should be addressed and considered separately.

[15] Release, at p.28.

[16] Courts and the SEC have stated that a person "effects" a securities transaction if they participate in "key points in the chain of distribution" of such transaction. *See* Mass. Fin. Servs., Inc. v. Sec. Inv'r Prot. Corp., 411 F. Supp. 411, 415 (D. Mass.), *aff'd*, 545 F.2d 754 (1st Cir. 1976), *cert. denied*, 431 U.S. 904 (1977); *see also* Transfer Online, SEC Denial of No-Action Request (May 3, 2000); David W. Blass, Chief Counsel, Division of Trading and Markets, SEC, Remarks to American Bar Association, Trading and Markets Subcommittee (Apr. 5, 2013) ("David Blass Speech"), available at https://www.sec.gov/news/speech/2013-spch040513dwghtm. Such activities have typically been viewed to include, among others, marketing securities, soliciting or negotiating and handling customer funds and securities. *See* David Blass Speech.

clarifying that certain basic written communications may be prepared and provided to investors by Tier II Finders as part of their limited solicitation-related activities.

C. Requirement to Not Perform "Due Diligence" Activities

The Proposed Exemption would not allow Finders to engage in any "due diligence" activities.[17] The Committee again believes that this restriction is overbroad. It could prevent a Tier II Finder educating herself as to the issuer or the potential investment in order to properly screen and have well-informed discussions with prospective investors. Such basic due diligence activities should be encouraged and would be entirely aligned with protecting the interests of investors. Moreover, due diligence activities by themselves are not broker activities that would otherwise require registration as a broker-dealer,[18] and there are persons, including lawyers and accountants, who routinely assist in due diligence activities without running afoul of the broker-dealer registration requirements. Further, it would be in the interest of the Finder to perform at least basic due diligence regarding the issuer and the relevant security in order to ensure that it is appropriately identifying and mitigating any liability risks that could arise in connection with the transaction. The Committee also notes that the M&A Broker Letter does not impose a similar restriction on M&A Brokers. For all of these reasons, the Committee suggests eliminating the requirement that Finders not perform "due diligence" in connection with a transaction.

D. Requirement to Not Assist Issuers in Structuring the Transaction or Negotiating the Terms of the Offering

The Proposed Exemption would not permit Finders to assist issuers in structuring or negotiating the terms of the offering.[19] Footnote 92 to the Release states that the "terms of the offering" would be interpreted as "the amount of securities offered, the nature of the securities, the price of the securities and the closing date of the offering period".[20] The Committee believes that this restriction is not necessary to protect investors and would unnecessarily hinder the ability of Finders to assist issuers in raising capital.

The smaller issuers that will be most likely to use and need the services of a Finder will be most likely to need outside help in structuring and negotiating transactions. Such small issuers will likely not be familiar with the various alternatives available for an offering. This is especially likely to be the case in geographic areas that lack robust venture capital and angel investor networks and for traditionally underrepresented founders, such as women and minorities, which the Release states the Proposed Exemption is intended to benefit.[21] It will be difficult for many such founders to make use of contacts provided by the Finder without receiving assistance in

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17 Release, at p.28.
18 *See supra* note 16.
19 Release, at p.28.
20 Release, note 92 on p.28.
21 *See* Release, at p.5.

structuring and negotiating the transaction. More likely than not, many small issuers will not want to engage Finders for the discrete task of locating investors for an offering for which the terms are fully-baked. Rather, they will need help to determine the most appropriate financing for their business needs and then assistance in locating sources for that financing .

E. Other Exchange Act Requirements That Apply to Broker-Dealers

The Release states that, in addition to not being required to register with the SEC as a broker, Finders "would not be subject to broker-dealer sales practice rules, including Regulation Best Interest."[22] The Release also states that Finders would continue to be obligated to comply with all other applicable laws, including the antifraud provisions of the Securities Act of 1933 (the "Securities Act") and the Exchange Act.[23] The Release does not expressly state, however, that Finders also would be exempt from other broker-dealer requirements under the Exchange Act, such as net capital or recordkeeping requirements, that do not specify whether the broker-dealer is required to be SEC-registered. We believe that an exemption from such requirements could be efficiently achieved by exempting Finders who come within the scope of the Proposed Exemption from the definition of "broker" under the Exchange Act, rather than just the requirement to register as a broker.[24]

F. Requirement to be a Natural Person

The Release provides that the Proposed Exemption would be available only to natural persons.[25] The Committee does not believe that limiting the exemption to natural persons is necessary. It is routine for small businesses to operate through wholly-owned limited liability companies or corporations. The use of such entities for tax and liability reasons is understandable and we see no reasonable justification for imposing such a limitation on Finders.

While we recognize that Rule 3a4-1 under the Exchange Act ("Rule 3a4-1"), can only be utilized effectively by "natural persons" (and, in particular, persons who are partners, officers, directors or employees of an issuer or its affiliates), the Committee sees no rationale for extending this limitation to the present context. Rule 3a4-1 was enacted to permit natural persons associated with an issuer and who meet certain other conditions, to engage in limited marketing activities without having to register as a broker-dealer under the Exchange Act, and the Rule did not need to expressly include issuers or other entities in order to accomplish its goals.[26] In this case, we do not believe that limiting the exemption to natural persons provides any particular benefit to issuers, investors or other market participants. Rather, such a limitation would limit potential tax planning

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22 Release, note 87 at p.26.

23 Release, at p.29.

24 In line with the SEC's note on p.29 of the Release, Finders would still continue to be subject to the antifraud provisions of the Securities Act and the Exchange Act.

25 *See* Release, at p. 17.

26 Persons Deemed not to Be Brokers, SEC Release No. 34-20943 (May 9, 1984).

and liability mitigation approaches for Finders without any corresponding investor protection or market integrity function. Accordingly, the Committee does not believe that it is necessary to limit the Proposed Exemption to natural persons.

G. State Regulation

As recognized in the Proposed Exemption, relief from the federal securities laws is never the end of the story.[27] Although the Committee believes that the Proposed Exemption will be an important step forward in bringing further clarity to this area, effective clarity cannot be achieved until state securities regulators take steps to coordinate with the Proposed Exemption. Accordingly, the Committee strongly supports the SEC's efforts to coordinate with state regulators in connection with the Proposed Exemption to ensure a workable nationwide solution to these longstanding challenges, and to provide clarity and consistency on the activities of Finders.[28]

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[27] *See* Release, at p.36 (asking whether the SEC should "coordinate with other regulators to provide clarity and consistency on what types of activities Finders and other limited purpose brokers may engage in").

[28] For example, following the SEC staff's lead in the 2014 M&A Broker Letter, in 2015 the North American Securities Administrators Association (NASAA) adopted a model M&A Brokers exemptive rule available at https://www.nasaa.org/wp-content/uploads/2011/07/MA-Broker-Model-Rule-adopted-Sept-29-2015-corrected.pdf .

We greatly appreciate the opportunity to provide comments with respect to this important rule-making effort and thank the SEC staff for its efforts and thoughtful approach to the issues addressed by Proposed Exemption. Members of the Drafting Committee are available to meet and discuss these matters with the SEC and FINRA staff and to respond to any questions.

Very truly yours,

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