

**PROPOSED SEC RULES
REGULATING “M&A BROKERS” AND
INTERMEDIARIES IN SMALL BUSINESS SALES**

(Updated 3/20/08)

Introduction

The Alliance of Merger and Acquisition Advisors (“*AM&AA*”), in conjunction with other professional associations of mergers and acquisitions intermediaries and business brokers (“*M&A Brokers*”), offers the following rules language (the “*Federal M&A Broker Rules*”) for consideration by the Securities and Exchange Commission (“*SEC*” or “*Commission*”). The proposed federal rules would be complemented by state-level rules and related regulation (the “*State M&A Broker Rules*”) that have been proposed to the North American Securities Administrators Association (“*NASAA*”).¹ Together, these federal and state rules would create a regulatory regimen for M&A Brokers as described in the Concept Outline For a Proposed Federal Broker Registration Exemption For Certain Business Brokers and M&A Intermediaries (Rev. 3/17/07) (the “*Concept Outline*”).² The Concept Outline explains in greater detail the rationale and impetus behind the proposed Federal and State M&A Broker Rules. That explanation will greatly aid in understanding the context of these proposed rules.

A primary objective of the Federal and State M&A Broker Rules is to enhance investor protection by improving understanding and compliance with federal and state securities laws. This would be accomplished by creating a new classification of “broker” under the Securities Exchange Act of 1934, as amended (the “*Act*”), in coordination with state securities laws, that will appropriately regulate the securities-related activities of M&A Brokers in mergers, acquisitions, and business brokerage transactions (“*M&A transactions*”) in view of the limited scope of their activities and the public interest in facilitating the free flow of capital to and from existing small business owners.

This proposed rulemaking ranked among the top three recommendations of the Final Report of the 2006 SEC Government-Business Forum on Small Business Capital Formation and similar recommendations were made in the reports from the 2004 and 2005 Forums. The proposed rules would complement other regulatory reforms to benefit small businesses announced by the SEC on May 23, 2007, Proposed Modernization of Smaller Company Capital-Raising and Disclosure Requirements, Press Release 2007-102. If the proposed rules are adopted, small business sellers and buyers would be better assured of receiving assistance from legitimate, compliant professional advisors in their sale transactions. The number of small business sale transactions has been increasing as baby boomers seek to retire and liquidate what is typically their single largest investment. While most of those transactions are legally structured as asset sales which are generally outside the scope of federal and state securities regulation, some of those transactions involve securities and, accordingly, are within the jurisdictional scope of those laws and related rules. It is critically important to understand that most, if not all, *M&A Brokers* primarily handle asset sale transactions but, in order to properly advise and serve their

¹ The proposed Federal and State M&A Broker rules have been shared with both the SEC and NASAA.

² The Concept Outline and the Comparison of Current and Proposed Regulation of Broker-Dealer Activities can each be downloaded from the AM&AA’s website at: <http://www.amaonline.com/amArticle.asp>

clients' needs and objectives, also need to be able to handle transactions where the sale of a business or business unit is accomplished through the sale of securities. In light of that, the proposed regulatory regimen is designed to be efficient and cost-effective for both regulators and *M&A Brokers*.

Another objective of the Federal and State M&A Broker Rules is to create a uniform system of state rules, to coordinate with the federal rule, so that the system of regulation is well defined and commonly understood by M&A Brokers, business buyers and sellers, their accountants, legal and financial advisers, and the general public. Uniformity will also aid in efficient administration of the rules and reduce costs for regulators and regulated persons. Therefore, the Commission's rules would be complemented at the state level through model rulemaking coordinated through NASAA and recommended for adoption by the states. This rulemaking proposal is patterned after the bifurcated regulatory model created by Congress, and implemented by the SEC and the states, for the regulation of investment advisers pursuant to the National Securities Markets Improvement Act of 1996. We believe this regulatory regimen can be created by federal and state rules within the agencies' existing statutory authority.

As explained in the Concept Outline, an M&A Broker could act as a "broker" in connection with the sale of all or part of an existing business that was effected through a stock purchase/sale, exchange, merger, or other business combination involving the transfer or issuance of securities if the conditions of the rule are met. Those conditions would include, among others, an annual notice filing or registration with those states having jurisdiction over the intermediary under state securities laws.

As illustrated in the AM&AA's Comparison of Current and Proposed Regulation of Broker-Dealer Activities (Rev. 3/17/07), the Federal and State M&A Broker Rules would require simplified state-level regulation for M&A Brokers whose securities-related activities go beyond the "baseline" recognized by the SEC's historical no-action letters, notably including the recent letter to *Country Business, Inc.*, 2006 SEC No-Act. LEXIS 669 (Nov. 8, 2006). That no-action letter has defined the circumstances when in connection with a small business sale an intermediary is not acting as a "broker" for purposes of the Act. Proposed Rule 15a-[], [*Intermediaries in Small Business Sale Transactions*] would, among other things, codify this no-action letter and aid in the public's understanding of its application. Under the Federal and State M&A Broker Rules the intermediary could not, however, be involved in capital raising from passive investors. New capital-raising activities in private placements could come within the scope of activities envisioned for a "private placement broker" as has been recommended by, among others, the ABA Private Placement Broker Task Force and the Final Report of the Advisory Committee on Smaller Public Companies dated April 23, 2006, or would otherwise require full broker-dealer registration and regulation under current law.

New investor protections relevant in the context of M&A transactions are built into the proposed rule. For example, the Federal and State M&A Broker rules require written engagements between the M&A Broker and its clients and the delivery of written disclosures, including business background information and conflicts of interest. Specific unethical business practices are enumerated in the rules. Most of these standards exist today only as ethical codes

of conduct adopted by some of the leading national and regional professional associations, but which do not have the force of law and so do not provide small business sellers and buyers with a full measure of protection because many intermediaries are not members of any professional association and today operate entirely outside of any regulatory oversight or guidance. The non-exclusive list of prohibited practices would be deemed to violate antifraud prohibitions in federal and state securities laws.

The proposed rules are intended to bring clarity to the current application of federal and state securities laws and rules to these activities. Currently, in the context of small business M&A transactions, securities laws and rules are widely ignored by thousands of intermediaries, accounting firms, legal counsel, and the public because their application in this context is so poorly understood, largely irrelevant, and extraordinarily burdensome in relation to the economics of the underlying activities and transactions. The perception of investor protection for small business sellers and buyers under today's regulatory system is illusory—at best it provides an expensive, time-consuming, after-the-fact remedy to redress egregious cases. Small business owners cannot afford the transaction fees that are necessary to support compliance with today's regulatory system, so either go without professional assistance or must use intermediaries who are not compliant. This proposal is intended to proactively address that reality and, as importantly, assure law-abiding intermediaries that their conduct is appropriate.

Finally, for the reasons more fully articulated by the American Bar Association's Private Placement Broker-Dealer Task Force,³ we recommend that, for a reasonable period of time after rulemaking, the state registration process should not focus on prior unregistered activities by requiring affirmative representations or attestations about historical activities—sometimes called “come clean” letters. A number of states do not presently impose such registration-related requirements but others insist upon it. No public purpose is advanced by imposing an industry-wide burden of analyzing thousands of historical transactions under federal and state securities laws in order to represent that there have been no prior unlawful unregistered activities. It is important to emphasize that, apart from registration issues, any prior acts of misconduct punishable under antifraud prohibitions would not be excused. If the SEC or a state regulator later learns of improper conduct by reason of complaint or inspection, the full range of regulatory powers is available to investigate and address those compliance issues.

Commission Authority

The Federal M&A Broker Rules would be adopted pursuant to the Commission's exemptive authority under the Act. Section 15(a)(2) of the Act authorizes the Commission to exempt any class of brokers from the registration requirements of Section 15(a)(1). Similarly, Section 15(b)(9) authorizes the Commission to exempt any class of brokers from the self-regulatory organization membership requirements of Section 15(b)(8) of the Act.

³ Part II, Section V, *Encouraging Registration*, Report and Recommendations of the Task Force on Private Placement Broker-Dealers, 60 Business Lawyer 959 (May 2005).

Section 15(c)(3) of the Act directs the Commission to establish minimum financial responsibility requirements for all brokers and dealers regardless of registration status. Accordingly, in conjunction with the Federal M&A Broker Rule, an amendment to Rule 15c3-1 is proposed defining the minimum financial responsibility requirements of an M&A Broker.

Most of the books and records requirements imposed under Section 17 of the Act and related SEC rules pertain to brokers registered under the Act. Since an M&A Broker would not be federally registered, conditions to the Federal M&A Broker Rule would include simplified books, records, and retention requirements relevant to the nature of their limited securities activities. Subsection 17(f)(1) imposes requirements with respect to lost and stolen securities and does not itself appear to include specific exemptive authority; however, given the limited nature of an M&A Broker's activities, if it is within the Commission's general authority, an exemption from these requirements is requested. Subsection 17(f)(2) imposes requirements with respect to fingerprinting and does grant the Commission exemptive authority. An exemption from the fingerprinting requirements is appropriate because M&A Brokers would not be permitted to have custody or possession of clients funds in any form or securities exchanged by the parties in the transaction.

In order to create a more uniform system of securities regulation, in Section 15(h) of the Act Congress preempted the states from imposing requirements for brokers-dealers that differ from, or are in addition to, the requirements in specified areas. Section 15(h) provides that:

No law, rule, regulation, or order, or other administrative action of any State or political subdivision thereof shall establish capital, custody, margin, financial responsibility, making and keeping records, bonding, or financial or operational reporting requirements for brokers, dealers, municipal securities dealers, government securities brokers, or government securities dealers that differ from, or are in addition to, the requirements in those areas established under this title. The Commission shall consult periodically the securities commissions (or any agency or office performing like functions) of the States concerning the adequacy of such requirements as established under this title.

(Emphasis added). In order to best assure uniformity, consistency, and efficiency in the application and administration of the proposed rules, each of these areas is addressed in the proposed *Federal M&A Broker Rule*. The Commission's consultation and coordination with the states is critical to developing and adopting these federal and state rules because the proposed system of regulation depends upon federal and state cooperation.

Many concepts and significant parts of the language used in the proposed rules were derived from existing federal and state securities laws and rules regulating both broker-dealers and investment advisers because an M&A Broker's engagements typically reflect a blend of those activities. For example, many disclosure concepts come from federal and state rules regulating investment advisers. The definition of a "Legal or Disciplinary Event" and related

disclosures of disciplinary events was adapted from the SEC’s Rule 206(4)-4, *Financial and Disciplinary Information that Investment Advisers Must Disclose to Clients*. The definition of a “Regulatory Disqualification” pulls terminology used in SEC rules and adds state law disqualifications. Many of the listed unethical business practices were adapted from existing state law concepts involving securities and real estate transactions. As a result, we believe the resulting rule proposals would better serve and protect small business sellers and buyers by focusing existing laws and rules in a uniform way that everyone can understand and apply in practice. The proposals also cost-effectively scale regulatory requirements recognizing that a substantial number of transactions handled *M&A Brokers* never involve securities.

For convenience of reference, all defined terms are self-contained within the proposed Federal M&A Broker Rule, rather than breaking them out into separate rules under Section 3(b) of the Act. Explanatory footnotes have been included as an aid to understanding. Italicized text appearing in brackets are the headings of other subsections in the rule, which are provided as an aid to understanding the cross-references.

Proposed Rule 15a-[] — Limited Exemption of Certain “M&A Brokers”

Preliminary Note: Since the U.S. Supreme Court’s opinion in *Landreth Timber Co. v. Landreth*, 471 U.S. 681; 105 S. Ct. 2297 (May 28, 1985), the federal securities laws have been applied to the sale of stock of a company. When an intermediary is engaged in the business of effecting the sale of businesses through the sale of stock or otherwise involving securities transactions, the intermediary may come within the definition of a “broker” under the Securities Exchange Act of 1934, as amended (“*Act*”). As such, a substantial body of laws and related regulations, as well as self-regulatory organization rules, have historically applied to the intermediary and have required, among other things, registration with the Commission and membership in a self-regulatory organization. State securities laws apply similar requirements. This rule applies the applicable federal securities laws in a manner which balances the public interest in investor protection with the public interest in assuring that small business sellers and buyers have affordable access to the services of a professional intermediary to assist them with the sale or purchase of a business.

This rule creates and regulates a “broker” classification that is referred to as an “*M&A Broker*.” An *M&A Broker*, as defined in this rule, is a person who is acting as a “broker” under the Securities Exchange Act of 1934, as amended (“*Act*”), in connection with the sale or purchase of all or part of an existing business involving the transfer, exchange, or issuance of securities in a *Qualified M&A Transaction*, as defined in the rule. Ownership of the business to be acquired may not be represented by any class of securities that are registered, or are required to be registered, with the Commission under Section 12(g) of the *Act* or with respect to which the issuer files periodic information, documents, and reports under Section 15(d) of the *Act*.

This federal rule exempts an *M&A Broker* from registration with the Commission as a “broker” under Section 15(a)(1) of the *Act* if specified conditions are satisfied. Among those conditions is the *M&A Broker’s* compliance with applicable state securities rules that are designed to complement the federal exemption. An *M&A Broker* is exempt from membership in

a registered securities association, such as the Financial Industry Regulatory Authority (“*FINRA*”) (f/k/a the National Association of Securities Dealers, Inc. (“*NASD*”). The financial responsibility obligations of an *M&A Broker* are specified in Rule 15c3-1[(f)].

Because an *M&A Broker* is not registered with the Commission, it is not subject to those provisions of the *Act* and the Commission’s rules that are made specifically applicable to a “registered broker or dealer” including, for example, the recordkeeping and retention requirements imposed under Section 17. Instead, separate books, records, and retention requirements are imposed among the conditions to this rule. The rule also requires, among other things, the *M&A Broker* to disclose important information about its business, its management, its affiliates, and any conflicts of interest and to retain those written disclosures among its books and records.

The rule contains a description of unethical business practices that are deemed to violate the anti-fraud prohibitions of the federal securities laws, including, Section 10 of the *Act* and Rule 10b-5. This list of practices is not exclusive; other practices or conduct may be deemed to violate applicable federal and state securities laws and rules.

The related Rule 15a-[__], [*Intermediaries in Small Business Sale Transactions*], codifies existing guidance provided by the SEC staff’s no-action letter to *Country Business, Inc.*, 2006 SEC No-Act. LEXIS 669 (Nov. 8, 2006). This no-action letter addressed scenarios where the transfer of ownership of a small business begins as an asset sale, generally not subject to the jurisdiction of securities laws, but later changes to the sale or exchange of stock or other securities to convey ownership. This no-action letter has defined circumstances where the intermediary is not deemed to be acting as a “broker” for purposes of the *Act* when an asset sale converts to a securities transaction.

Finally, under the Investment Advisers Act of 1940, as amended (“*Advisers Act*”) the term “investment adviser” covers “any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities.” This defined term excludes from its scope “any broker . . . whose performance of such services is solely incidental to the conduct of his business as a broker . . . and who receives no special compensation therefor.” Accordingly, typically, an *M&A Broker* or other intermediary who advises a client about the value of a business in connection with the purchase or sale of a business would not be deemed to be an “investment adviser” under the *Advisers Act*. Under the conditions of the rule an *M&A Broker* may not, however, advise a client about the value of its securities if offered to the public or traded on a public market.

For ease of understanding, terms defined in this rule appear in italics. Otherwise, terms have the meanings assigned under the *Act* and the Commission’s rules.

(a) *M&A Broker Exemptions*. If all of the conditions in this rule are met, then with respect to a *Qualified M&A Transaction* as defined and described in paragraph (c) [*Nature of Engagement*]:

(1) An *M&A Broker* and its *associated persons* acting in their limited capacity described in this rule are exempt from the requirements imposed under the following sections of the *Act* —

- (i) registration with the Commission as a “broker” under Section 15(a)(1);
- (ii) membership in a registered securities association under Section 15(b)(8);
- (iii) obligations with respect to “penny stocks” under Section 15(g);
- (iv) the books and records requirements under Section 17;
- (v) reporting obligations with respect to missing, lost, counterfeit, or stolen securities under Section 17(f)(1); and
- (vi) fingerprinting with respect to its *associated persons* under Section 17(f)(2).

(2) An *M&A Broker* and its *associated persons* may engage in all of the securities-related activities described in paragraph (i) [*Permitted Activities*] but may not engage in the activities described in paragraphs (j) [*Prohibited Activities*] or (k) [*Unethical Business Practices*] of this rule.

(b) Conditions to the Exemptions. In order to qualify for the exemptions provided in paragraph (a) [*M&A Broker Exemptions*] of this rule, each of the following conditions must be met with respect to a *Qualified M&A Transaction*:

(1) The activities of the *M&A Broker* and its *associated persons* are performed with respect to a *Qualified M&A Transaction* in the manner described in paragraph (c) [*Nature of Engagement*] of this rule. The *M&A Broker’s* compliance with the conditions of paragraph (c) [*Nature of Engagement*] shall not be affected by any action independently taken by a *party*, such as changing the legal structure of the transaction in a manner that no longer meets the conditions of a *Qualified M&A Transaction* or involving new *parties* in the transaction.

(2) The *M&A Broker* provides its client with an *Engagement* described in paragraph (d) [*Terms and Conditions of the Engagement*] of this rule prior to any obligation of the client to the *M&A Broker* becoming legally binding on the client and prior to the receipt, directly or indirectly, of any money or other consideration from the client by the *M&A Broker* or any *associated person*. The *Engagement* may be subsequently supplemented, amended, or modified as expressly provided in the contract or as otherwise

agreed to by the *M&A Broker* and the client. If permitted under applicable state law,⁴ the *Engagement* may expressly provide that the *M&A Broker*, through one or more of its *associated persons*, is acting on behalf of one or more of the *parties* as an independent, dual, or limited intermediary, and not as an agent for a single principal in the *Qualified M&A Transaction* (a “*Modified Agency Capacity*”). The *Engagement* shall describe the role of the *M&A Broker* and its *associated persons* in a *Modified Agency Capacity*, their legal obligations to the *parties* to the transaction, and any limitations on those obligations as may be imposed contractually or under applicable state law.

(3) The *M&A Broker* delivers the written *Background and Conflict Disclosures* described in paragraph (e) [*Background and Conflict Disclosures*] of this rule to its client(s) before the *Engagement* becomes legally binding on the client. If the *M&A Broker* is acting in a *Modified Agency Capacity*, the *M&A Broker* delivers the *Background and Conflict Disclosures* to all known *parties* to the *Qualified M&A Transaction* not later than the time when those *parties* enter into a legally binding contract to consummate a *Qualified M&A Transaction*.

(4) The *M&A Broker* makes each required *Regulatory Filing* described in paragraphs (f) [*Home State Registration*] and (g) [*Notice Filing in Other States*] of this rule.

(5) Each *associated person* of the *M&A Broker* involved in the *Qualified M&A Transaction* meets all qualifications and requirements imposed under the *M&A Broker’s home state(s)* securities laws and related rules.

(6) The *M&A Broker* makes and maintains the books and records required by paragraph (h) [*Books and Records*] of this rule.

(7) The *M&A Broker* meets the financial responsibility requirements of Rule 15c3-1[(f)].

(8) With respect to the *Qualified M&A Transaction*, neither the *M&A Broker* nor any *associated person* of the *M&A Broker* has engaged in any prohibited or unethical business practice described in paragraphs (j) [*Prohibited Activities*] or (k) [*Unethical Business Practices*] of this rule.

(9) Neither the *M&A Broker* nor any *associated person* of the *M&A Broker* is subject to a *Regulatory Disqualification* as defined in paragraph (l) [*Definitions*] of this rule. With respect to any state law disqualifications, a state securities administrator may waive that disqualification, with or without imposing conditions on the individual’s par-

⁴ We have incorporated the concept of a *Modified Agency Capacity* to harmonize this rule with other state licensing laws. Real estate licensing laws in several states recognize and authorize modified agency relationships, including relationships referred to as “dual agency,” “transaction broker,” and “designated sales associate.” Such state licensing laws impose their own obligations and requirements with respect to these kinds of agency relationships. Adding this *Modified Agency Capacity* concept to the rule is not intended to itself create agency relationships that are not otherwise recognized by state laws.

participation in *Qualified M&A Transactions*, upon a satisfactory showing of good cause to grant such a waiver; provided, that such waiver is consistent with the public interest and the protection of investors.

(c) Nature of Engagement. The exemptions described in paragraph (a) [*M&A Broker Exemptions*] of this rule are available only with respect to activities that are related to a proposed or actual transaction, whether or not consummated, involving securities that meets all of the following conditions (a “*Qualified M&A Transaction*”):

(1) The *M&A Broker’s* services described in the *Engagement* pertain to the purchase or sale of a *Business*, regardless of the existing or resulting form of ownership or the legal structure used in the transaction to convey the ownership of the *Business* (e.g., sale of assets, exchange of securities, merger, or other business combination).

(2) One or more *Eligible Buyers* purchase, directly or indirectly, ownership of the *Business*.

(3) Ownership of the *Business* is not represented by any class of securities that is registered, or is required to be registered, with the Commission under Section 12(g) of the *Act* or with respect to which the issuer files periodic information, documents, and reports under Section 15(d) of the *Act*.⁵

(4) Only the *Business* is advertised or marketed for sale and not its securities. Advertising of the *Business* may use any form of public media including, for example, mailings, newspapers, magazines, and the Internet.

(5) Neither the *Business* nor the client is known by the *M&A Broker* to be a “public shell company” (i.e., any company whose securities are publicly traded on an exchange or over the counter but which no longer has any significant business operations) or any legal entity formed for the purpose of evading the registration or exemption requirements of the Securities Act of 1933, as amended, the *Act*, or the related rules.

(6) In determining the *M&A Broker’s* compliance with the conditions of this paragraph, the *M&A Broker* may rely upon representations made by a *party* in the *Engagement*, in any transaction-related document exchanged by the *parties*, or in any separate document signed by the *party* making the representations. The *M&A Broker* will not be deemed to have failed to meet a condition of paragraph (c) [*Nature of Engagement*] of this rule to the extent that a *party* refuses to provide the *M&A Broker* with any representation or documentation described in this rule. If for reasons beyond the control of the *M&A Broker* the conditions of this paragraph are no longer met with respect to an *Engagement*, the *M&A Broker’s* role from that point forward shall be limited to the following:

⁵ This would not preclude a *Business* from being acquired by a company whose securities are registered with the Commission under Section 12(g) of the of the *Act* or with respect to which the issuer files periodic information, documents, and reports under Section 15(d) of the *Act* where, for example, the consideration given to the seller are the buyer’s securities.

- (i) transmitting documents between the *parties*;
- (ii) valuing the assets of the *Business*;
- (iii) providing administrative support; and
- (iv) assisting the client with preparation of financial statements.

(d) Terms and Conditions of the Engagement. The *M&A Broker* shall provide the client with a written “**Engagement**” containing, at a minimum, the following information:

(1) A description of the *M&A Broker’s* services and any related deliverables that are material to those services.

(2) All of the material terms, conditions, and contingencies pertaining to the *M&A Broker’s* services and any related deliverables in connection with the *Qualified M&A Transaction*.

(3) The name(s) of the *party* or other payor, and the amount or manner of calculation, of all advances, deposits, fees, charges, compensation, and expense reimbursements to be paid to the *M&A Broker*, directly or indirectly, fixed or contingent, in connection with the *Qualified M&A Transaction*. The *M&A Broker’s* compensation may be a fixed amount or a percentage of the transaction’s value, or may be related to the post-closing performance of the *Business*, and may be contingent upon a successful consummation of the transaction regardless of the transaction’s structure (i.e., whether structured as a transfer of assets or securities). The *M&A Broker’s* compensation may include securities (e.g., stock, options, or warrants), subject to all applicable requirements under federal and state securities laws.⁶

(4) If the *M&A Broker* is acting in a *Modified Agency Capacity* as described in paragraph (e)(12), the consent of each *party* to the *M&A Broker’s* role in the transaction as disclosed in the *Engagement* or the *Background and Conflict Disclosures*.

(5) A provision stating that there cannot be an assignment of the *Engagement* by the *M&A Broker* without the prior consent of the client. A transaction which does not result in a change of actual control or management of the *M&A Broker* is not an “assignment” for purposes of this paragraph.

(6) If the *M&A Broker* is legally organized as a partnership, a provision stating that the client will be promptly notified of any material change in the membership of the partnership.

⁶ Securities received by an *M&A Broker* as compensation could be registered stock or could be restricted stock depending on the relevant facts and circumstances, so the rule does not attempt to characterize what restrictions or limitations may apply under applicable securities laws and rules.

(e) *Background and Conflict Disclosures*. The “***Background and Conflict Disclosures***” required by paragraph (b) [*Conditions to Exemptions*] of this rule contain, at a minimum, the following information and may contain additional information so long as the required content remains conspicuous. The disclosures may be delivered in paper or in electronic formats so long as a client is able to retain a copy. The required content includes:

(1) The legal and any assumed names of the *M&A Broker*, its state of organization or domicile, its primary business address, its primary telephone number, its website (if any), and the name of a person who can be contacted for further information.

(2) Background information about the *M&A Broker*, including how long it has been in business, the names of its directors, principal officers, managers, or partners, and the name of any affiliated business that may become involved, directly or indirectly, in the *Qualified M&A Transaction*.

(3) A general description of the *M&A Broker’s* primary and any related ancillary business services.

(4) The name of each *associated person* of the *M&A Broker* who will have primary responsibility for performing the services described in the *Engagement* and describing the person’s education; business background and employment for at least the prior five years; professional credentials and designations; and all current regulatory registrations, licenses, examinations, and other qualifications.

(5) A description of all known and reasonably anticipated roles, relationships, direct or indirect compensation, economic interests, referral relationships, and other conflicts of interest that the *M&A Broker* or its *associated persons* may have with respect to the *M&A Broker’s* client or any other person involved with the *Qualified M&A Transaction*.

(6) A description of any control or ownership relationships, directly or indirectly, between or among the *M&A Broker* and any of the *parties*, lenders, or service providers to the *Qualified M&A Transaction*.

(7) A description of any *Legal or Disciplinary Event* that resulted in a penalty, sanction, judgment, or award against the *M&A Broker* or a *management person* of the *M&A Broker* during the prior 10 years that is material to an evaluation of the integrity of the *M&A Broker* or a *management person*, or the *M&A Broker’s* ability to perform the *Engagement*, including the date and nature of the action, the agency, court, or arbitration forum, and the result and/or sanction imposed.

(8) A statement that the *M&A Broker* is “relying upon a federal exemption from broker registration under the Securities Exchange Act of 1934 with the United

States Securities and Exchange Commission” and providing the Commission’s current headquarters address, telephone number, and Internet website address.

(9) A statement that the *M&A Broker* is “subject to the securities laws and related rules in the state or states where it is headquartered or has an office, and may be subject to other state securities laws and rules;” and the name, address, telephone number, and Internet website address of the state securities agency in each state where it is headquartered or has an office.

(10) The *M&A Broker* may identify itself in the disclosure document, and may hold itself out to the public, as being a “state registered M&A broker” or a “state registered M&A advisor” if it complies with the requirements of this rule.

(11) Cautionary statements to the effect that:

(i) The client is encouraged to seek legal counsel before advancing any money, disclosing any nonpublic documents, or entering into any legally binding contracts or agreements, either oral or written, such as the *Engagement*, a confidentiality agreement, a letter of intent, or an agreement to buy or sell some or all of a business, its ownership, or its assets.

(ii) The *M&A Broker* may or may not, as applicable, have independently verified some or all of the information provided by one *party* to any other *party* to the transaction.

(iii) The *M&A Broker* is not a member of a self-regulatory organization such as the Financial Industry Regulatory Authority (f/k/a National Association of Securities Dealers, Inc.).

(iv) The disclosures have not been reviewed or approved by the Commission or any state securities agency or self-regulatory authority.

(v) Registration of the *M&A Broker* or its *associated persons* under applicable state securities law requirements does not, in and of itself, imply that the *M&A Broker* possesses any specified level of skill, training, or experience, except as may be prescribed by state law or related rules.

(12) If permitted under applicable state law and expressly provided in the *Engagement*, the *M&A Broker* is acting in the *Qualified M&A Transaction* in a *Modified Agency Capacity*, then statements that:

(i) Neither the *M&A Broker* nor any of its *associated persons* considers any single *party* to the transaction to be its “principal” under state agency law. The *M&A Broker* and its *associated persons* will treat each of the *parties* to the

transaction fairly and equitably, and will not favor one *party*'s interests over another.

(ii) The *Engagement* contains all of the material terms and conditions related to the *M&A Broker's* role in the transaction with respect to the *parties*.

(iii) All compensation to be received, directly or indirectly, by the *M&A Broker* and its *associated persons* in connection with the transaction has been fully disclosed to all *parties*.

(iv) The *parties* are encouraged to consult with their own legal counsel or independent financial advisors with respect to the *Engagement* and the transaction.

(v) Are specifically prescribed by applicable state law.

(13) The most current effective or revision date of the disclosures.

(f) Home State Registration. In order to register under paragraph (a) [*M&A Broker Exemptions*] of this rule, an *M&A Broker* shall make a "**Regulatory Filing**" with the administrator in each state or states in which its home office and any branch office are located or in which it regularly and systematically conducts business involving securities that is subject to this rule (its "**home state(s)**"). The *Regulatory Filing* shall be made annually. The *Regulatory Filing* shall be made and consist of all of the following:

(1) The legal and any assumed names of the *M&A Broker*, its state of organization or domicile, its primary business address, its primary telephone number, its website (if any), and the name of a person who can be contacted for further information.

(2) A balance sheet reporting the *M&A Broker's* assets, liabilities, and ownership equity, demonstrating that the *M&A Broker* is solvent. The balance sheet shall be —

(i) dated as of a date not less than 45 days prior to the date of the filing with the *M&A Broker's home state(s)*;

(ii) certified by the *M&A Broker's* chief executive officer as being true and accurate in all material respects.

(iii) prepared or compiled by an independent public accountant; provided, if the *M&A Broker* requires from a client an advance, deposit, retainer, or prepayment of fees or reimbursable expenses of more than \$50,000 more than six months in advance of earning some or all of the fees or incurring the reimbursable expenses determined in the manner prescribed in the *Engagement*, then it shall be either reviewed or audited by an independent public accountant.

- (3) With respect to each *associated person* of the *M&A Broker* —
- (i) his or her name and any known assumed names or aliases;
 - (ii) his or her ownership interest, if any, in the *M&A Broker*;
 - (iii) his or her current residential address, date of birth, social security number, and starting date with the *M&A Broker*; and
 - (iv) any individual identification number(s) issued by or on behalf of a registered securities exchange, a registered securities association, or a state regulatory agency.
- (4) With respect to the *M&A Broker* and all *associated persons* of the *M&A Broker*, a signed certification by the *M&A Broker's* chief executive officer that, to the best of his or her knowledge after reasonable inquiry —
- (i) no *associated person* is subject to a *Regulatory Disqualification*; and
 - (ii) no *associated person* has been subject to a *Legal or Disciplinary Event*, except as described in the *Regulatory Filing*.
- (5) A copy of the *M&A Broker's* current *Background and Conflict Disclosures* and generic samples of the customary form or forms typically used in its *Engagements*.
- (6) Payment of the fee or fees applicable to the *Regulatory Filing* prescribed by the administrator.
- (g) *Notice Filings in Other States*. With respect to any state, other than its *home state(s)*, having jurisdiction with respect to the *M&A Broker* or a *Qualified M&A Transaction*, the *M&A Broker* shall make a “***Notice Filing***” with the administrator at the earlier to occur of (i) entering into an *Engagement* with a client located in that state or (ii) the closing of a transaction in, or involving a *party* located in, that state or as soon thereafter as the *M&A Broker* is notified that the closing has occurred. For purposes of complying with this rule, no *Notice Filing* shall be required in any state that has not adopted under its securities law a rule implementing the state-level requirements of this rule. The *Notice Filing* shall, if necessary, be made annually. The *Notice Filing* shall be made and consist of all of the following:
- (1) A duplicate copy of the *Regulatory Filing* made with its *home state(s)*, which shall be filed with the administrator not less than five business days prior to the closing of the transaction.

(2) The balance sheet filed with the M&A Broker's *home state(s)* certified by the *M&A Broker's* chief executive officer as then continuing to represent the financial condition of the *M&A Broker* in all material respects. If there has been a material adverse change in the M&A Broker's financial condition since the original date of the balance sheet, then the *M&A Broker* shall file a new balance sheet as of a date not less than 45 days prior to the filing, certified by the *M&A Broker's* chief executive officer as being true and accurate in all material respects.

(3) Payment of the fee or fees applicable to the *Notice Filing* prescribed by the administrator.

(h) Books and Records. An *M&A Broker* shall make and maintain the following books and records, which shall be preserved and made available promptly upon request for inspection by the Commission's staff and state regulatory agencies having jurisdiction over the *M&A Broker* for not less than six years, the first two years in an easily accessible place:⁷

(1) Each version of the *Background and Conflict Disclosures*, including all amendments and supplements, as delivered to a client or *party* to a transaction.

(2) A list of all *Engagements*, including the names and addresses of the *parties* and the date of each transaction's closing.

(3) The *Engagement* and the *Background and Conflict Disclosures*, including all related amendments and supplements, delivered to each client of the *M&A Broker*.

(4) The following records with respect each *Qualified M&A Transaction* (to the extent that these documents are provided to the *M&A Broker* by a *party*):

(i) All legally binding agreements, including amendments and supplements, among the *parties* to the transaction.

(ii) The principal closing documents, including documents used to convey title and ownership of the *Business* and evidencing the transmittal or delivery of the consideration exchanged by the *parties*.

(iii) Evidence demonstrating that the transaction meets the conditions of paragraph (b) [*Conditions to Exemptions*] of this rule.

(iv) Records of the receipt, directly or indirectly, of all compensation by the *M&A Broker* and its *associated persons* with respect to the transaction.

⁷ To aid in the common understanding and application of the proposed rule, all of the applicable recordkeeping requirements are contained in this rule rather than incorporating them through cross-references to provisions in Rules 17a-3 and 17a-4.

(5) Each of the *M&A Broker's* check books, account statements, and reconciliations with respect to each bank, brokerage, mutual fund, or other custodial account used in connection with its securities-related business activities.

(6) A compliance manual describing the requirements and prohibitions of this rule and those aspects of federal and state securities laws and related rules that are applicable to the *M&A Broker's* activities, and including a statement of policies and procedures reasonably designed to assure compliance with those requirements by the *M&A Broker* and its *associated persons*.

(7) An application or questionnaire for employment (such as a FINRA Form U-4) executed by each *associated person* of the *M&A Broker*, reviewed and approved in writing by its authorized representative, and containing at least the following information with respect to the *associated person*:

(i) The *associated person's* name, any assumed names or aliases, current and last residential address, date of birth, social security number, and the starting date of the *associated person's* employment or other association with the *M&A Broker*.

(ii) A complete, consecutive statement of all the *associated person's* employment for at least the preceding ten years, noting whether such employment was part time or full time.

(iii) A list of all registrations, qualifications, and licenses held with any registered securities exchange, registered securities association, or state regulatory agency under securities or insurance laws during the preceding ten years, including the individual's identification number issued by or on behalf of the association or agency (such as the FINRA's Central Registration Depository).

(iv) A certification that the *associated person* is not subject to any *Regulatory Disqualification*, except as specifically described in the certification with related documentation attached.

(v) A certification that the *associated person* has not been subject to a *Legal or Disciplinary Event*, except as specifically described in the certification with related documentation attached.

(8) Any deliverable document from the *M&A Broker* to a client that is specifically identified in the *Engagement* (such as a business appraisal).

(9) A file containing all written complaints from clients or *parties* to a *Qualified M&A Transaction* objecting to the conduct, activities, or services performed by the *M&A Broker* or its *associated persons*.

(i) Permitted Activities. Insofar as compliance with federal securities laws are concerned,⁸ if the conditions to this rule are met, an *M&A Broker* and its *associated persons* may engage in any activities not prohibited by this rule or other applicable laws, rules, or regulations⁹ with respect to a *Qualified M&A Transaction* without being registered with the Commission as a “broker” under the *Act*, including, without limitation:

(1) Advise a client about the value of the *Business*, the price, the terms, the legal structure for the transaction, tax implications, and other transaction-related matters; and advise a client about one or more purchase offers, including the terms, amount and form of consideration, and all other aspects of the proposal.

(2) Prepare, or help prepare, and communicate with *parties* to the transaction, an information package or other documents with respect to the *Business* containing some or all of the following without limitation: business description, its history, historical financial statements, pro forma financials, current ownership structure, organization, management, owners’ and management’s objectives with respect to on-going involvement, seller’s motivation, willingness of the seller to finance, preferred transaction structure, forecast, what is included/excluded in the sale, price expectations, and valuation of the *Business*.

(3) In a “sell-side” *Engagement*, identify prospective *Eligible Buyers* and advertise and market the sale of a *Business* to *Eligible Buyers*, other intermediaries, professional advisors (e.g., lawyers, accountants, and bankers), using private and public media such as mailings, newspapers, magazines, and the Internet; provided, that the *M&A Broker* screens inquiries and only proceeds with those persons who are reasonably believed to be *Eligible Buyers* or their authorized representatives.

(4) In “buy-side” *Engagements*, identify and communicate with prospective sellers to determine their interest in a transaction.

(5) In all *Engagements*, contact and meet with the prospective *parties* to obtain or provide information about the *Business* and the prospective *parties*.

(6) Negotiate the price, terms and conditions, legal structure, and other matters with respect to the transaction with or on behalf of a client.

(7) Draft or participate in drafting, or communicate terms sheets, letters of intent, offers, counteroffers, and definitive purchase agreements or other documents on be-

⁸ Other federal, state, and local laws, rules, and ordinances may also apply, such as professional licensing for the practice of law or accountancy. This exemption does not alter or affect registration, licensing, or other requirements applicable to other types of businesses or transactions under other federal or state laws such as may be applicable to a business broker, real estate broker, mortgage broker/lender/servicer, bank, or insurance producer or agency.

⁹ These permitted activities are provided by way of examples to aid in the common understanding of this rule and its effects in light of existing guidance issued by the Commission and the staff. This list is not exhaustive of permissible activities related to *Qualified M&A Transactions*.

half of its client; provided, however, that, for an *M&A Broker* to engage in these specific activities, legal counsel shall also be involved in closing the transaction unless the aggregate consideration to be exchanged is reasonably believed to be valued at less than \$500,000.

(8) Organize and assist with the preparations or performance of any due diligence investigation with respect to the *Business* or the *parties* to the transaction.

(9) Suggest or recommend sources of possible commercial financing to a buyer; provided, that the *M&A Broker* has no role and does not receive compensation of any kind with respect to a securities offering to finance any part of the transaction.

(10) Conduct or assist with the closing of the transaction, including the delivery of closing documents; provided, that the *M&A Broker* must not have actual or constructive custody, possession, or handle any funds in any form (including such forms as cash, checks, and money orders)¹⁰ or securities exchanged by the *parties* in the transaction.

(11) Analyze, model, or project the revenues, expenses, and financial performance of the *Business*, proposed payment terms and any contingencies, or the proposed structure of the transaction including, for example, evaluating historical and projected revenues and expenses, financial modeling and forecasting, benchmarking with comparable businesses and transactions, appraising the *Business's* assets and liabilities, cash flow analyses, and similar financial matters; provided, that these activities do not include or involve any analysis of the *Business's* stock value or performance in public securities markets.

(12) Prepare financial and analytical reports and models pertaining to the *Business* and its operations; provided, that the *M&A Broker's* work product conspicuously states that it is intended only for internal use by the client or the parties to the transaction and use by their counsel, accountants, bankers, and other professional advisors, and by *Eligible Buyers* in a *Qualified M&A Transaction*.

(13) Prepare or assist with a client's proposal and/or application to obtain a commercial loan from a bank, commercial lender, or financing sources other than involvement with a securities offering to raise debt or equity to finance the transaction.

(14) Receive compensation from referral and fee-sharing arrangements with registered brokers and dealers or other brokers operating under this or any other exemption from registration under the *Act*, provided that the compensation is fully disclosed as provided in this rule and subject to compliance with all applicable laws and rules, and

¹⁰ Current federal law requires a broker-dealer to have a minimum net capital of \$50,000 in order to handle client checks or securities. Annual independently audited financial statements are also required, together with a schedule calculating the firm's net capital.

self-regulatory organization bylaws and rules, pertaining to such referrals and related compensation.¹¹

(15) Receive compensation from banks, appraisers, title companies, insurance agencies, and other nonsecurities-related, third-party service providers, provided that the compensation is fully disclosed as provided in this rule and subject to compliance with all applicable laws, rules, or regulations pertaining to referrals in those contexts (e.g., insurance licensing).

(j) Prohibited Activities. An *M&A Broker* and its *associated persons* may not engage in any of the following activities in reliance upon this rule:

(1) Make or participate in any offer or sale of securities other than pursuant to this rule to any person other than (i) an *Eligible Buyer*, (ii) the seller or other person employed in a management capacity with respect to the *Business* who receives restricted securities as transaction-related consideration or for future services, or (iii) the *M&A Broker* or its *associated persons* who receives restricted securities as consideration for their services.

(2) Have actual or constructive custody or possession of funds or securities of a buyer, seller, or other *party* to the *Qualified M&A Transaction*. This shall not prohibit an advance, deposit, retainer, or prepayment of fees or reimbursable expenses; provided, that if the amount is more than \$50,000 and is received more than six months in advance of earning some or all of the fees or incurring the reimbursable expenses determined in the manner prescribed in the *Engagement* those funds shall be deposited until earned by the *M&A Broker* in a segregated account separately identified as being for the benefit of the *M&A Broker's* clients at an insured depository institution.

(3) Exercise discretionary authority to legally bind a buyer, seller, or *party* to any legal obligation, or to close a *Qualified M&A Transaction*. This does not prohibit an *M&A Broker* from having an express written direction and power of attorney to act on behalf of a *party* within the explicit limitations on that authority.

(k) Unethical Business Practices. The following is a non-exclusive list of business practices which are deemed to constitute a violation of Section 10(b) of the *Act* and Rule 10b-5 by an *M&A Broker* or its *associated persons*.

(1) The *M&A Broker* or an *associated person* shall not, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails —

¹¹ For example, NASD Rule 2420 presently limits referral fees being paid by members to non-members. This is a rule which historically was based on a concern about the non-member being engaged in an activity for which broker-dealer registration was required. The ability for fully-registered broker-dealers to pay, and state-registered M&A Brokers to receive, referral fees would facilitate the free flow of clients and their transactions among intermediaries, offering different levels of services, skills, professional expertise, and associated fees and costs.

- (i) employ any device, scheme, or artifice to defraud;
 - (ii) make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; or
 - (iii) engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.
- (2) The *M&A Broker* or an *associated person* fails to fully and accurately disclose to any client or prospective client all material facts with respect to:
- (i) any financial condition or circumstance of the *M&A Broker* or an *associated person* that is reasonably likely to impair the *M&A Broker's* ability to meet contractual commitments to clients if the *M&A Broker* requires an advance, deposit, retainer, or prepayment of fees or reimbursable expenses of more than \$50,000 more than six months in advance of earning some or all of the fees or incurring the reimbursable expenses determined in the manner prescribed in the *Engagement*;
 - (ii) a *Legal or Disciplinary Event* that is material to an evaluation of the integrity of the *M&A Broker's* or any *management person* of the *M&A Broker* or the ability of the *M&A Broker* to perform the *Engagement*; or
 - (iii) any information required to be disclosed by paragraph (e) [*Background and Conflict Disclosures*] of this rule in its *Background and Conflict Disclosures*.
- (3) The *M&A Broker* or an *associated person* fails to —
- (i) protect and promote the best interests of its client;
 - (ii) inform or otherwise ensure disclosure to the client of any material information which the *M&A Broker* or its *associated person* knows, or in the exercise of reasonable care should know based on the information furnished to the *M&A Broker*, is material to the client's decision-making with respect to a transaction; the *M&A Broker* is not required to independently generate nor verify information provided by a client or by another *party*, provided that the *M&A Broker* discloses to all recipients the extent of, or limitations upon, any investigation performed with respect to the information;
 - (iii) fully disclose all of its conflicts of interests;

(iv) timely deliver all bona fide written offers or counteroffers received by the *M&A Broker* to the client and disclose all known information pertaining to the offer or counteroffer that would be material to the client's decision making with respect to the offer or counteroffer; and timely deliver any written counteroffer as directed by the client; and

(v) disclose to the client if a "buy-side" *Engagement* is not exclusive and that the *M&A Broker* or an *associated person* may also represent one or more other potential *parties* to a possible transaction with respect to the *Business* and the circumstances under which it may do so.

(4) The *M&A Broker* or an *associated person* shall not —

(i) favor its own interests or the interests of any *party* over the client or, if acting in a *Modified Agency Capacity*, favor one *party* over another *party* without full disclosure and authority from each *party*;

(ii) disclose the client's confidential information to another person without the client's authorization;

(iii) make a loan to the client or to another *party* for the purpose of funding any part of a transaction without fully disclosing the existence of the loan to all *parties*;

(iv) make an appraisal of the *Business* that is outside or beyond the scope of the *M&A Broker's* experience without either (A) obtaining the assistance of an authority on such types of property; or (B) disclosing the extent or lack of the *M&A Broker's* experience to the client;

(v) make an appraisal or render an opinion of value on any *Business* when the *M&A Broker* has a present or contemplated interest unless such an interest is specifically disclosed in the appraisal; the *M&A Broker's* employment or fee may not be contingent upon the amount of an appraisal;

(vi) take any action by or on behalf of a client (A) without having authority from the client to do so in the *Engagement* or otherwise; or (B) that is contrary to the explicit written instructions of the client with respect to that matter;

(vii) accept any form of compensation from any person other than the client with respect to an *Engagement* without fully disclosing the compensation in writing to the client;

(viii) misrepresent the person's educational record, professional background, experience, track record or successes with respect to other transactions, or

business relationships with the intent to induce the client to engage the *M&A Broker*; or

(ix) misrepresent the number or qualifications of the professional or staff employed by, or affiliated or associated with the *M&A Broker*, with the intent to exaggerate the true size, scope, experience, or capabilities of the *M&A Broker*.

(l) Definitions. Italicized terms not otherwise defined in this rule have the following meanings for purposes of this rule:

(1) An “*associated person*” of an *M&A Broker* includes —

(i) any partner, officer, director, manager, or trustee (or any person occupying a similar status or performing similar functions) with respect to the *M&A Broker*;

(ii) any person directly or indirectly controlling, controlled by, or under common control with the *M&A Broker*; and

(iii) any employee, independent contractor, or other authorized representative of such broker, but excepting any person whose functions are solely clerical or ministerial.

(2) A “*Business*” means a business, business unit, business line, division, department, or specific assets held by a sole proprietorship, corporation, limited liability company, partnership, business trust, or other legal entity for use in connection with the operation of a commercial enterprise.

(3) An “*Eligible Buyer*” includes all of the following:

(i) An individual who, besides acquiring an ownership interest in the *Business*, will —

(A) be personally and actively engaged in the governance, management, and operation of the *Business* following a *Qualified M&A Transaction* in the capacity of a corporate director or senior officer, a member or manager of a limited liability company, a general partner of a partnership, a trustee of a business trust, a sole proprietor, or a position of similar involvement with the *Business*;

(B) alone, or acting in concert with others, control the governance, management, and operations of the *Business*; and

(C) have access to substantially all of the *Business's* financial, accounting, tax, and other books and records.¹²

(ii) A member of the immediate family (parent, spouse, sibling, or child) of an individual described in the preceding subparagraph (i).

(iii) A trust the primary beneficiary of which is any individual described in the preceding subparagraphs (i) and (ii).

(iv) An existing business entity (including a sole proprietorship).

(v) An existing venture capital fund, an equity fund, the sponsor of such a fund, a business development company, a small business investment company, or any similar entity.

(vi) A corporate entity or entities formed to facilitate the transaction that is owned and controlled by a person described in the preceding subparagraphs (i), (ii), (iii), (iv), or (v). In determining who is an *Eligible Buyer* one or more related steps taken for a business purpose proximately in time to a *Qualified M&A Transaction's* closing will be viewed as a whole.

(vii) An employee stock ownership plan as defined in Section 4975(e)(7) of the Internal Revenue Code of 1986, as amended, for the benefit of some or all of the employees of the *Business*.

(4) “**Legal or Disciplinary Event**” means any of the following events involving the *M&A Broker*, a *management person*, or an *associated person* that was not resolved in the person’s favor, or were not subsequently reversed, suspended, vacated, or expunged:

(i) A criminal or civil action in a court of competent jurisdiction or an arbitration forum in which the person —

(A) was convicted, pleaded guilty or nolo contendere (“no contest”) to a felony or misdemeanor, or is the named subject of a pending criminal proceeding involving an *investment-related* business; fraud, false statements, or omissions; wrongful taking of property; or bribery, forgery, counterfeiting, or extortion;

(B) was *found* to have been *involved* in a violation of an *investment-related* statute or regulation; or

¹² An *Eligible Buyer* need not be an “accredited investor.” Some small business buyers would not qualify as such and this rule is intended to benefit them too.

(C) was the subject of any order, judgment, or decree permanently or temporarily enjoining the person from, or otherwise limiting the person from, engaging in any *investment-related* activity or being associated with any broker-dealer, investment adviser, bank, or other financial institution.

(ii) Administrative proceedings before the Commission or any other federal regulatory agency or any state regulatory agency in which the person —

(A) was *found* to have caused an *investment-related* business to lose its authorization to do business; or

(B) was *found* to have been *involved* in a violation of an *investment-related* statute or regulation and was the subject of an order by the agency denying, suspending, or revoking the authorization of the person to act in, or barring or suspending the person's association with, an *investment-related* business; or otherwise significantly limiting the person's *investment-related* activities.

(iii) Proceedings by a *SRO* in which the person —

(A) was *found* to have caused an *investment-related* business to lose its authorization to do business; or

(B) was *found* to have been *involved* in a violation of the *SRO's* rules and was the subject of an order by the *SRO* barring or suspending the person from membership or from association with other members, or expelling the person from membership; fining the person more than \$2,500; or otherwise significantly limiting the person's *investment-related* activities.

(iv) Disciplinary proceedings by any professional association, educational institution, or other organization suspending or revoking a professional credential, designation, attainment, or license to use its professional trademarks.

(5) When used in this rule in the context of a *Legal or Disciplinary Event* —

(i) a “*management person*” means a person with power to exercise, directly or indirectly, a controlling influence over the management or policies of the *M&A Broker* or to determine the advice or recommendations given to a client;

(ii) “*found*” means determined or ascertained by adjudication, award, or consent in a final *SRO* proceeding, administrative proceeding, or court action;

(iii) “**investment-related**” means pertaining to securities, commodities, banking, insurance, or real estate (including, but not limited to, acting as or being associated with a broker-dealer, investment company, investment adviser, government securities broker or dealer, municipal securities dealer, bank, savings and loan association, entity or person required to be registered under the *Act*, the *Advisers Act*, or the Commodity Exchange Act [7 U.S.C. § 1, et seq.], or fiduciary); and

(iv) “**involved**” means acting or aiding, abetting, causing, counseling, commanding, inducing, conspiring with, or failing reasonably to supervise another in doing an act.

(6) An “**M&A Broker**” is a person (either corporate or natural) who is acting as a “broker” as defined in the *Act* in connection with the sale of all or part of an existing *Business*, including stock purchases, exchanges, mergers, acquisitions, and business combinations involving the transfer or issuance of securities in a *Qualified M&A Transaction*. The term does not include a person who is acting as an intermediary or business broker in connection with a transaction described in Rule 15a-[], [*Intermediaries in Small Business Sale Transactions*].

(7) A “**party**” or “**parties**” to a *Qualified M&A Transaction* is the person or persons who are signatories to the Engagement or are identified as signatories to a definitive agreement to consummate the transaction as a buyer or seller and who are specifically identified as such to the *M&A Broker*.

(8) A “**Regulatory Disqualification**” means the person is or was —

(i) subject to a Commission order issued under Section 15(b)(4) of the *Act*;

(ii) subject to a Commission order issued under Section 203(f) of the *Advisers Act*;

(iii) convicted within the previous ten years of any felony or misdemeanor involving conduct described in Section 203(e)(2)(A) through (D) of the *Advisers Act*;

(iv) found by the Commission to have engaged, or has been convicted of engaging, in any of the conduct specified in paragraphs (1), (5), or (6) of Section 203(e) of the *Advisers Act*;

(v) subject to an order, judgment, or decree described in Section 203(e)(4) of the *Advisers Act*; or

(vi) subject to an order issued by an administrator under a state’s securities laws, or by a SRO under its bylaws or rules, to—

(A) revoke or suspend the registration or membership of the person as a broker-dealer, agent, investment adviser, investment adviser representative; or

(B) bar the person from association with a broker-dealer or investment adviser as a partner, officer, director, agent, representative or person having a similar status or performing similar functions with a broker-dealer or investment adviser, or from directly or indirectly controlling a broker-dealer or investment adviser.

(9) A “***Self-Regulatory Organization***” or “***SRO***” means any national securities or commodities exchange, registered association, or registered clearing agency.

Proposed Amendment to Rule 15c3-1 — Net Capital Requirements for Brokers or Dealers

Amend Rule 15c3-1 by adding a new Section [(f)] as follows:

[(f)] Sections (a), (d), and (e) of this rule shall not apply to an “*M&A Broker*” as defined in, and who conducts business in accordance with, Rule 15a-[] *Exemption of Certain “M&A Brokers”*. Instead, an *M&A Broker* shall be subject to the following requirements:

- (1) The *M&A Broker* must at all times be financially solvent.
- (2) The *M&A Broker* must make and maintain the financial books and records prescribed by Rule 15a-[] — *Limited Exemption of Certain “M&A Brokers.”*
- (3) The *M&A Broker* shall immediately cease all operations, notify the Commission and each state securities agency having jurisdiction if it ceases to be solvent, and not recommence operations unless and until —
 - (i) the *M&A Broker* is solvent in all respects; and
 - (ii) the *M&A Broker* has re-submitted its *Regulatory Filing* with each state securities agency having jurisdiction.
- (4) An *M&A Broker* is not permitted to have actual or constructive custody or possession or to handle a client’s funds in any form (including such forms as cash, checks, and money orders) or securities.
- (5) There is no minimum capital requirement nor a bonding requirement for an *M&A Broker* operating in compliance with Rule 15a-[] — *Limited Exemption of Certain “M&A Brokers.”*
- (6) There is no periodic financial reporting requirement for an *M&A Broker* operating in compliance with Rule 15a-[] — *Limited Exemption of Certain “M&A Brokers.”*

Proposed Rule 15a-[], [Intermediaries in Small Business Sale Transactions]

Preliminary Note: This rule codifies historical guidance provided by the SEC staff’s no-action letter to *Country Business, Inc.*, 2006 SEC No-Act. LEXIS 669 (Nov. 8, 2006). This no-action letter addressed the role of an intermediary where the transfer of ownership of a small business begins as an asset sale, generally not subject to the jurisdiction of securities laws, but later changes into the sale or exchange of stock or other securities to convey ownership. Upon such a change in the legal structure of the transaction, an intermediary who conforms its activities regarding transactions described in this rule is not covered under the definition of a “broker” under the *Securities Exchange Act of 1934* (the “Act”) and is exempt from registration and other requirements applicable to a broker under the Act, including registration as an “M&A Broker” or a “Private Placement Broker” as those terms are used in Rules [] and [].

This exclusion from broker registration and related regulation does not affect the application of the antifraud provisions of federal securities laws to securities-related activities.

Exclusion From Definition of a “Broker.” If all of the conditions in paragraphs (b) through (f) of this rule are met, then a person acting as an Intermediary in connection with the sale or purchase of a business consummated as a conveyance of stock or other securities is not deemed to be a “broker” as defined in Section 3(a)(4) of the *Act* (15 U.S.C. 78c(a)(4)), an “M&A Broker” under Rule [], or a “Private Placement Broker” under Rule [].

(a) **Definition of Intermediary.** The term “Intermediary” means a person who engages in the activities described in paragraphs (b) through (f) of this rule.

(b) **Sale of a Small Business.** The business to be sold is a corporation, limited liability company, proprietorship or partnership which satisfies the size standards for a “small business” pursuant to the Small Business Size Regulations issued by the U.S. Small Business Administration, as those regulations may be amended from time to time. The business to be sold is a going concern and not a “shell” organization. The business, as a whole, or its assets are advertised or otherwise offered for sale, and the Intermediary will not promote the sale of securities. If the transaction is effected by means of the transfer, exchange, or issuance of securities, then all of the business’s equity securities are conveyed to a single buyer or group of buyers formed without the assistance of the Intermediary.

(c) **Intermediary’s Role.** The Intermediary is engaged to act as an agent of a seller, a buyer, controlling equity holders, or, to the extent permitted by state law, in the capacity of an independent, dual, or limited agent regarding multiple parties in connection with the transfer of ownership of the business. The Intermediary does not advise the parties whether to issue securities, or otherwise to effect the transfer of the business by means of securities, or assess the value of any securities sold (other than by valuing the assets of the business as a going concern). The Intermediary may prepare a detailed description of the business to be sold based on information supplied by the parties, including historical financial data, and publicly available information; provided, however, that the Intermediary apprise potential purchasers that the Intermediary makes no representations about the accuracy of the information provided.

(d) Intermediary's Compensation. The Intermediary's compensation in connection with the transaction is determined prior to the parties' decision on how to effect the transfer of ownership of the business and does not vary according to the legal structure of the conveyance (i.e., securities rather than sale of assets). The compensation may be calculated as a fixed fee, an hourly fee, a commission, or a combination thereof, that is based upon the consideration received by the seller. The compensation may be deferred to the same extent that the consideration paid by the buyer to the seller is deferred. If consideration to the seller from the buyer is paid in part at closing, and in part after closing, the Intermediary may likewise receive its compensation in part at, and in part after, closing. The amount of compensation may depend on the occurrence or nonoccurrence of future events. The formula to compute the compensation is fixed prior to the determination of whether to structure the transaction as a sale of the seller's assets or a sale of securities.

(e) Intermediary's Activities in a Securities Transaction. After the parties decide to effect the transaction through a sale of securities, instead of a sale of assets, thereafter:

(1) The Intermediary limits its services to: (i) transmitting documents between the parties; (ii) valuing the assets of the business as a going concern; (iii) providing one or more of the parties with administrative support; and (iv) assisting with the preparation or analysis of the business's financial statements;

(2) The Intermediary does not have or exercise the power to bind any party in the transaction;

(3) The Intermediary does not have custody or possession of funds of the parties in the transaction.

(f) Involvement with Financing. The Intermediary does not assist a buyer in obtaining financing, other than providing uncompensated introductions to third-party lenders and helping a buyer with preparing the paperwork and financial statements associated with loan applications.