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SEC ISSUES NO-ACTION LETTER CLARIFYING TREATMENT OF UNREGISTERED M&A BROKERS

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The Background

M&A practitioners have long faced uncertainty as to whether persons who facilitate mergers, acquisitions, business sales and business combinations ("M&A transactions") were required to be registered as broker-dealers under either federal or state law. Because, under federal law, an M&A transaction effected in the form of a stock sale constitutes the "sale of a security" subject to the federal securities laws, financial advisory professionals have long found themselves in the situation where a client's transaction, if effected as an asset sale, poses no regulatory concern, while the identical transaction in the form of a stock sale could expose both the advisor and the transaction to regulatory risk. State broker-dealer regulations present a complex patchwork of definitions and exemptions for brokers, "dealers", "finders" and the like, and the SEC's guidance in the area has been very narrow – until now.

Recent No-Action Relief

The SEC's Division of Trading and Markets, in a recent no-action letter (**M&A Brokers**, January 31, 2014), has given meaningful guidance and clarity to unregistered financial advisors involved in M&A transactions. The staff created a definition of "M&A Broker", being a person engaged in the business of effecting securities transactions solely in connection with the transfer of ownership and control of a privately-held company to a buyer that will actively operate the company. The guidance further defines a "privately-held company" as a company that does not have securities registered under the Exchange Act and is not otherwise obligated to file periodic Exchange Act reports, and gives some examples of how it would evaluate the meaning of "actively operate". The staff takes the position that it would not recommend enforcement if an unregistered "M&A Broker" engaged in an M&A transaction that took the form of a stock sale.

The no-action relief goes far beyond the SEC's previous guidance on permitted activities of "finders". The new guidance does not place any limitations on an M&A Broker receiving transaction-based compensation or on many of the customary financial advisory activities in which it can permissibly engage. The guidance does place restrictions on the nature of the underlying transaction as to which the relief is intended to apply, principally to attempt to ensure that the activity is a "true" M&A transaction and not a disguised securities offering or the like.

Good News, But Only a Beginning

The no-action letter provides a welcome clarification as to the applicability of federal broker-dealer registration requirements to financial advisors providing M&A transaction services. Welcome as the guidance is, however, it does not relieve the burden of untangling, and attempting to comply with, the array of state securities regulations and their application to "brokers", dealers" and "finders". Whether and to what extent the states follow the lead of the SEC remains to be seen, but the clarity on this issue at the federal level is a major development for M&A practitioners and advisors.

If you have any questions regarding this recent securities law development or would like any further information regarding any of the matters discussed above, please contact one of the individuals listed in this publication.

Contacts

Daniel G. Berick
+1 216 479 8374
daniel.berick@squiresanders.com

Abby E. Brown
+1 703 720 7894
abby.brown@squiresanders.com

Robert E. Gregg
+1 703 720 7880
robert.gregg@squiresanders.com

Fred A. Summer
+1 614 365 2743
fred.summer@squiresanders.com

Frank M. Placenti
+1 602 528 4004
frank.placenti@squiresanders.com