Broker-Dealer Regulation: New Developments and Continuing Practical Concerns Regarding Registration Requirements for Business Brokers, "Finders," and Other Financial Intermediaries

By Stephen P. Wink, Dana G. Fleischman, and Brett M. Ackerman

Stephen P. Wink is a partner in the New York office of Latham & Watkins LLP.*

Dana G. Fleischman is a partner in the New York office of Latham & Watkins LLP.**

Brett M. Ackerman is an associate in the Washington, D.C. office of Latham & Watkins LLP***

The past year brought significant developments relating to business brokers, placement agents and others who act as financial intermediaries. Recent guidance from the staff of the Division of Trading and Markets (Staff) of the Securities and Exchange Commission (SEC) has shed new light on the types of activities that may (and may not) require certain financial intermediaries to register as broker-dealers under Section 15(b) of the Securities Exchange Act of 1934 (Exchange Act). In addition, the Financial Industry Regulatory Authority, Inc. (FINRA) has issued to its members a notice regarding a proposed reduced rule-set that would apply to brokerage firms solely engaged in limited corporate finance activities.

As discussed below, although these developments should provide a measure of relief to a number of market participants, it does not offer the solution that many financial intermediaries – particularly those in the private fund space – were hoping for. Accordingly, we expect to see further movement in this area as the private fund industry and other interested parties continue to engage the regulators in a dialogue regarding broker-dealer registration requirements and the appropriateness, in the absence of such registration, of certain types of compensation arrangements and other sell side activities.

Background

Section 15(a) of the Exchange Act requires that persons engaged in broker or dealer activity register with the SEC pursuant to Section 15(b) of the Exchange Act unless an applicable exemption is available.[1] In general, a "broker" is any person "engaged in the business of effecting transactions in securities for the account of others and a "dealer" is any person "engaged in the business of buying and selling securities for such person's own account."[2] Although the Exchange Act and the rules promulgated thereunder do not specifically define "effecting transactions" or "engaged in the business," the SEC and the Staff have taken a very expansive view of the scope of those terms. Based on no-action guidance from the Staff, activities that may be

©2014, Stephen P. Wink, Dana G. Fleischman, and Brett M. Ackerman

deemed (alone or in combination) to confer "broker" status include, among other things:

- Soliciting investors to enter into securities transactions;
- Assisting issuers in structuring prospective securities transactions or helping issuers to identify potential purchasers of securities;
- Participating in the negotiating process or otherwise bringing buyers and sellers of securities together; and
- Receiving compensation contingent on the success of a securities transaction or based on the amount or value of a securities transaction.[3]

Activities that have been identified (alone or in combination) by the Staff as indicators of "dealer" status include, among other things:

- Participating in a selling group, underwriting securities or purchasing or selling securities as principal from or to customers rather than from or to only brokers or dealers;
- Carrying a dealer inventory (positions intended to be used directly or indirectly to trade with customers) or holding oneself out as a dealer or market-maker or as otherwise willing to buy or sell particular securities on a continuous basis;
- Obtaining a regular clientele of customers, issuing or originating securities or rendering incidental investment advice to others; and
- Engaging in trading transactions for the benefit of others (including for an affiliate or for an affiliate's customers), rather than consistently with one's own judgment and investment and liquidity objectives.[4]

Among the activities outlined above, the Staff has consistently viewed transaction-based compensation as the "hallmark" of broker-dealer activity and has typically required that any person who receives such compensation (or any fee based on the "success" of a securities transaction) be registered as a broker-dealer. In particular, the Staff has stated that:

> [T]he receipt of compensation related to securities transactions is a key factor that may require an entity to register as a broker-dealer. Absent an exemption, an entity that receives securities commissions or other transaction-based compensation in connection with securities-based activities that fall within the definition of "broker" or "dealer" generally is itself required to register as a broker-dealer. Registration helps to ensure that persons who have a "salesman's stake" in a securities transaction operate in a manner that is consistent with customer protection standards governing broker-dealers and their associated persons. That principle not only encompasses the individual who directly takes a customer's order for a securities transaction, but also any other person who acts as a broker with respect to that order, such as the employer of the registered representative or any other person in a position to direct or influence the registered representative's securities activities.[5]

While the Staff has taken an extremely expansive view of the concept of being "engaged in the business," some courts have been more lenient in this regard, finding that something more than just transaction-based compensation is necessary to require broker-dealer registration.[6] The Staff's position on the matter, however, makes paying transaction-based compensation to financial intermediaries in connection with a securities transaction largely untenable in the absence of specific guidance or no-action relief given the legal risks of engaging an unregistered broker-dealer discussed below.

In only very limited circumstances, the Staff has permitted certain financial intermediaries to receive transaction-based compensation without registering as broker-dealers. For example, in the early 1990s, the Staff granted no-action relief to an individual whose involvement in securities transactions was limited to one instance of providing a list of names and telephone numbers of potential investors and receiving a success fee for doing so.[7] This no-action position gave rise to the notion that a so-called "finder's exemption" exists in the law and lore under the Exchange Act. Nonetheless, despite this very limited fact pattern, the Staff has effectively disavowed this no-action position (although it has not been formally withdrawn) and has indicated that it would not likely issue the letter today.[8]

The Staff has also agreed not to recommend enforcement under the Exchange Act in regard to an intermediary who was to receive transaction-based compensation in connection with an acquisition that began as an asset sale and later was structured as a stock deal.[9] Although it is clear that the sale of non-securities assets should not implicate the Exchange Act's broker-dealer registration requirements, once the sale of a security becomes involved in the transaction, the requirement may be triggered. This no-action letter permitted the intermediary to receive a fee if it essentially backed away from significant participation in the transaction once the securities element was present. Of course, this and other related

requirements in the no-action letter significantly limited the utility of the relief for many market participants.

Recent Developments

On January 31, 2014, the Staff issued a no-action letter (M&A No-Action Letter) permitting certain "M&A Brokers" to facilitate securities transactions in connection with the purchase and sale of privately-held companies and receive transaction-based compensation without registering as broker-dealers under Section 15(b) of the Exchange Act.[10] The M&A No-Action Letter follows a pair of no-action letters issued to AngelList[11] and FundersClub[12] in March 2013, which indicate a certain thawing of the Staff's views on what constitutes broker-dealer activity for purposes of the registration requirements of Section 15(a) of the Exchange Act. In the 2013 no-action letters, relief was granted for investment advisers to promote their offerings via an online platform. Notably, however, the critical element upon which the relief was based was that no compensation was to be paid to the investment advisers that could be deemed "transaction-based." The M&A No-Action Letter, thus, marks the first time in recent memory that the Staff has permitted transaction-based compensation to be received by persons who arguably fall within the definition of "broker" under the Exchange Act, but are not registered as such.

Recent guidance from the [SEC] staff has shed new light on the types of activities that may (and may not) require certain financial intermediaries to register as broker-dealers under Section 15(b) of the … Exchange Act….

The M&A No-Action Letter also follows a public speech on April 5, 2013 by David Blass, Chief Counsel of the Division of Trading and Markets, in which Blass discussed the potential application of the broker-dealer registration requirements in connection with private placements and other services for private funds.[13] Although the M&A No-Action Letter does not provide any direct answers to the issues cited by Blass, he indicated the Staff's willingness to work with the private fund industry in an effort to address these concerns. He also indicated that among the options the SEC was considering was working collaboratively with FINRA on a more customized approach for regulation of market participants who perform only limited broker-type functions. At the same meeting in which Mr. Blass delivered his April 5, 2013 speech, Robert Colby, Chief Legal Officer of FINRA, similarly indicated that FINRA was reviewing its rules in order to develop a more streamlined approach for members that participate in certain limited types of brokerage activities. And, on February 26, 2014, FINRA issued a request for comment on its first proposal in this regard—specifically, a more narrow set of membership and conduct rules that would apply to member firms solely performing limited corporate finance activities.[14]

The M&A No-Action Letter

Scope of the M&A No-Action Letter

Since at least the formation of the ABA Task Force on Private Placement Broker-Dealers in the mid-2000s,[15] there has been a concerted effort by practitioners in the small business arena to convince the SEC to provide relief for business brokers and others involved in the purchase and sale of small businesses. The M&A No-Action Letter represents the fruit of these efforts, and grants relief to M&A Brokers facilitating mergers, acquisitions, business sales, and business combinations between buyers and sellers of "privately-held companies."

For purposes of the M&A No-Action Letter, the term "privately-held company" is defined as a company that does not have any class of securities registered, or required to be registered, with the SEC under Section 12 of the Exchange Act, or with respect to which the company files, or is required to file, periodic information, documents, or reports under Section 15(d) of the Exchange Act.[16] Additionally, the company must be an "operating company" that is a going concern and not merely a "shell company" with no or nominal operations and assets or assets consisting only of cash or cash equivalents.[17] The SEC staff specifically noted, however, that a "going concern" need not be profitable, and could even be emerging from bankruptcy, so long as it has actually been conducting business, including soliciting or effecting business transactions or engaging in research and development activities.[18]

Among other things, the transactions covered by the M&A No-Action Letter must satisfy the following criteria:

- The transaction must not involve a public offering of securities, and any offer and sale of securities in the transaction must be conducted in compliance with an applicable exemption from registration under the Securities Act of 1933 (Securities Act) and any securities received by the buyer or M&A Broker in connection with the transaction must be "restricted securities," as defined in Rule 144(a)(3) under the Securities Act;[19]
- The transaction must involve a sale to a buyer (or group of buyers) that will "control" the company and "actively operate" it at the conclusion of the transaction (passive buyers are expressly excluded). The M&A No-Action Letter defines "control" as the power, directly or indirectly, to direct the management or policies of a company, whether through ownership of securities, by contract, or otherwise. The necessary control will be presumed to exist if, upon completion of the transaction, the buyer or group of buyers has the right to vote 25 percent or more of a class of voting securities; has the power to sell or direct the sale of 25 percent or more of a class of voting securities; or in the case of a partnership or limited liability company, has the right to receive upon dissolution or has contributed 25 percent or more of the capital. A buyer may actively operate the company through the power to elect executive officers and approve the annual budget or by service as an executive or other executive manager, among other things;[20] and
- The M&A Broker must not have the ability to bind a party to the transaction.[21]

The "actively operate" requirement will likely limit the utility of the M&A No-Action Letter for many situations, such as for private funds that take a minority stake in a company. Nonetheless, in transactions where control of the board of directors of the target is obtained, it would appear the active operation requirement would be satisfied.

Another important element of the relief that may serve to limit its utility—particularly for private funds and their affiliated advisers that seek to obtain transaction-based fees—is the requirement that the intermediary not have the ability to bind any parties to the transaction. That is, they must truly be an intermediary, rather than a principal in the transaction or another entity that has discretion or power of authority to act on the principal's behalf as is typically the case with affiliated advisers to private funds.

Specified Activities

To the extent the conditions cited in the M&A No-Action Letter are satisfied, M&A Brokers are permitted to engage in the following types of activities, among others, without having to register as a broker-dealer:

- Receive transaction-based compensation;
- Participate in negotiations (without the ability to bind either party to a transaction);
- Advertise the company for sale with information such as the description of the business, general location, and price range; and
- Advise the parties to issue securities or otherwise to effect the transfer of the business by means of securities (as opposed to an asset purchase/sale), or assess the value of any securities sold.[22]

The M&A No-Action Letter also makes clear that an M&A Broker may not provide financing for a transaction (either directly or indirectly), and that to the extent the M&A Broker assists purchasers in obtaining financing from an unaffiliated third party, the M&A Broker must comply with all applicable legal requirements and any compensation received by the M&A Broker must be disclosed to the client in writing.[23] To the extent securities-related financing is obtained for the transaction, the M&A No-Action Letter would not relieve an M&A Broker from the broker-dealer registration requirements to the extent its activities in connection with such financing would otherwise be captured under the Exchange Act.

Practical Considerations

Although some industry participants appear to have read more into the relief granted in the M&A No-Action Letter, it remains narrowly tailored and focused on the "business broker" constituency. The M&A No-Action Letter is also subject to a number of specific conditions, including the active management of the target and that the intermediary not have the ability to bind the parties to the deal. Accordingly, market participants that intend to rely on the M&A No-Action Letter should carefully review its terms to fully ascertain its scope, and should consider applicable state broker-dealer registration requirements, which continue to apply even if the proposed activities might otherwise fall within the parameters of the relief from federal broker-dealer registration requirements.

Issues Particular to Private Funds

Although private funds may rely on the M&A No-Action Letter in connection with utilizing the services of M&A Brokers, the requirements that the intermediary not have the ability to bind a party to the transaction and that the buyer actively operate the acquired business may act to limit the M&A No-Action Letter's utility for private funds, particularly in addressing the issues raised by Blass. In his April 2013 speech, Blass indicated that in connection with its examinations of newly-registered private fund advisers, the Staff has observed that (i) certain private fund advisers are paying transaction-based compensation to their personnel for selling interests in a fund and (ii) private fund advisers, their personnel and/or their affiliates are receiving transaction-based compensation "for purported investment banking or other broker activities relating to one or more of the fund's portfolio companies."[24] Reiterating that the SEC and the Staff have consistently viewed transaction-based compensation as the "hallmark" of broker-dealer activity, Blass cautioned that the receipt of transaction-based compensation coupled with the types of activities being performed may trigger the requirement to register with the SEC as broker-dealers under the Exchange Act.[25]

Blass noted that certain market participants have inquired regarding the application of Rule 3a4-1 under the Exchange Act (the so-called "issuer's exemption") in the context of private fund advisers.[26] That Rule provides that an associated person of an issuer (such as employees and directors of the issuer or its affiliates) may be exempt from the requirement to register as a broker or dealer under the Exchange Act to the extent he or she complies with the conditions outlined in the Rule. Among these conditions, however, is a requirement that the individual not receive transaction-based compensation. For that reason, employees, such as investor relations personnel, may not qualify for the exemption to the extent they receive commissions or bonuses based on the amounts raised. In that respect, Blass also specifically noted that private fund managers who pay employees transaction-based compensation for selling interests in a fund would not likely be able to avail themselves of the Rule 3a4-1 safe harbor.[27] It should also be noted that the exemption is only available to persons who have other substantive duties for the issuer and participate in an offering of securities no more than once every 12 months—which further limits the exemption's potential utility for many private funds.[28]

Potential Relief for Limited Corporate Finance Brokers

On February 26, 2014, FINRA issued Regulatory Notice 14-09, which set forth a proposed modified rule-set (Proposed Rules) that would apply to firms that fall within the definition of "broker" under the Exchange Act, but that engage in only a limited range of activities—namely, advising companies and private equity funds on capital raising and corporate restructuring.[29] Under the Proposed Rules, these firms, referred to as "limited corporate finance brokers" (LCFBs), would include any broker that *solely* engages in one or more of the following types of activities:

- advising an issuer, including a private fund, concerning its securities offerings or other capital raising activities;
- advising a company regarding its purchase or sale of a business or assets or regarding its corporate restructuring, including a going-private transaction, divestiture or merger;
- advising a company regarding its selection of an investment banker;
- assisting in the preparation of offering materials on behalf of an issuer;
- providing fairness opinions; and
- qualifying, identifying or soliciting potential institutional investors.[30]

LCFBs may not carry or maintain customer accounts, hold or handle customers' funds or securities, accept orders from customers to purchase or sell securities either as principal or as agent for the customer, possess investment discretion on behalf of any customer, or engage in proprietary trading of securities or market-making activities.[31]

An entity that seeks to qualify as an LCFB would follow the same procedures for membership as any other FINRA applicant. However, a FINRA member seeking to change its status to an LCFB, subject to certain conditions, could file a request to amend its membership agreement rather than filing a new application.[32]

Principals and representatives of an LCFB would also be subject to the same registration and qualification examination requirements as principals and representatives of other FINRA firms, but would be eligible for fewer registration categories.[33]

An LCFB firm's principals and representatives would be subject to most FINRA rules governing investigations, sanctions and disciplinary proceedings. However, the Proposed Rules would establish a more streamlined set of rules with respect to duties and conflicts, supervision and responsibilities related to associated persons, and financial and operational obligations. Presumably, this limited rule-set would decrease the overall cost of establishing and maintaining a registered entity to engage in corporate finance activities and thereby encourage additional participation in such activities by smaller entities that would otherwise be "priced out of the market" or risk engaging in such activities without being registered.

Although the Proposed Rules represent a promising framework, again there are at least two significant drawbacks. First, LCFBs may only deal with institutional investors (defined under FINRA rules to include, in addition to certain other institutional entities, any individual with assets of $50 million or more). Such a limitation could severely constrain the utility of this limited membership category for entities that solicit investors in private funds. FINRA made clear that it would not consider reducing this threshold to the accredited investor standard; however, it remains to be seen whether they could be convinced to lower the threshold to the more workable qualified purchaser standard under the Investment Company Act of 1940.[34] Such a change would dramatically improve the utility of the Proposed Rules and could substantially address the internal marketing issues raised by Blass. Second, LCFBs would be subjected to the same FINRA new membership application process as full-service broker-dealers. Thus, the overall path to registration is likely to remain long and arduous. In fact, the expense and length of the registration and FINRA membership process remains a significant barrier for many aspiring broker-dealers, regardless of their proposed business model.

Risks of Engaging Unregistered Financial Intermediaries

Blass' remarks together with recent SEC enforcement actions (discussed below) have placed the contours and consequences of paying transaction-based compensation to finders and other financial intermediaries that are not properly registered as brokers in stark relief. While Blass indicated a willingness on part of the Staff to consider exemptive relief for certain limited broker activities at some point in the future, and although the FINRA proposal represents a significant step in that respect, it is clear that private fund managers, early stage companies and others who may be involved in capital raising activities must carefully structure their arrangements to comply with applicable regulatory requirements as they exist today. Accordingly, company executives and fund managers should continue to be mindful of their arrangements surrounding capital raising activities, and be particularly wary of compensation agreements that may be construed as providing transaction-based compensation to persons not properly registered as broker-dealers under the Exchange Act and applicable state securities laws.

Recent Enforcement Actions

Employing unregistered financial intermediaries may expose companies, private fund managers and their principals to SEC enforcement actions – even where there are no allegations of fraud or other misconduct. For example, last year the SEC charged William M. Stephens (Stephens), Donald W. Phillips (Phillips) and Ranieri Partners LLC (Ranieri Partners) in connection with Ranieri Partners' capital raising efforts for two private funds (the Funds).[35] Phillips was a senior managing partner of Ranieri Partners and caused an affiliate of Ranieri Partners to retain Stephens as an "independent consultant" to find potential investors for the Funds.[36] Ranieri Partners agreed to pay Stephens a fee equal to one percent of all capital commitments made to the Funds by investors introduced by Stephens.[37]

Phillips was a long-time friend of Stephens and was "generally aware" that Stephens had a prior disciplinary history with the SEC. In fact, Stephens had been previously barred from the securities industry.[38] According to Phillips, he specifically informed Stephens that Stephens' activities on behalf of Ranieri Partners would be limited to simply contacting potential investors to arrange meetings for the principals of Ranieri Partners and that Stephens was not permitted to provide private placement memoranda directly to potential investors or to contact investors directly to discuss the merits or strategies of the Funds.[39] Nevertheless, the SEC found that, in fact, Phillips did very little to limit Stephens' activities and that Stephens actively solicited investors on behalf of the Funds.[40]

As a result of these activities, the SEC concluded that Stephens violated Section 15(a) of the Exchange Act by failing to register as a broker or dealer or as an associated person of a broker or dealer.[41] The SEC also found that Ranieri

Partners caused Stephens' violations of Section 15(a) of the Exchange Act because it failed to adequately oversee Stephens' activities.[42] Similarly, the SEC concluded that Phillips willfully aided and abetted Stephens' violations of Section 15(a) of the Exchange Act by failing to limit Stephens' activities, despite knowing that Stephens was to have a limited role in introducing potential investors.[43]

In only very limited circumstances, the Staff has permitted certain financial intermediaries to receive transaction-based compensation without registering as broker-dealers.

As part of the settlement, Stephens agreed to be permanently barred from the securities industry and to pay disgorgement and pre-judgment interest in excess of $2.8 million.[44] Ranieri Partners agreed to a civil money penalty of $375,000 and to cease and desist from causing any violations or future violations of Section 15(a) of the Exchange Act.[45] Phillips also submitted to a cease and desist order and agreed to a $75,000 civil penalty as well as a nine-month suspension from acting in a supervisory capacity in the securities industry.[46]

Investor Rescission Rights

In addition to enforcement risks, there are other serious consequences of employing financial intermediaries that are not properly registered, or exempt from registration, as broker-dealers. Significantly, Section 29(b) of the Exchange Act provides that contracts made in violation of the Exchange Act shall be void in respect of the "rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract." Thus, if a sale of securities is effected through an unregistered broker-dealer, investors may have the right to rescind their purchases.

Providing a potential "put" right to investors can have dire consequences. For example, Neogenix Oncology Inc. (Neogenix), a biotechnology firm, went public in 2010 and in late 2011, revealed that an inquiry by the SEC in connection with its periodic filings had uncovered that it had employed finders in its late stage capital raising efforts and that such persons were not properly registered under the Exchange Act as brokers.[47] As a result, Neogenix concluded that some of its investors may have the potential right to rescind their investments. These potential rescission rights, in turn, caused uncertainty regarding the accounting treatment of the company's liabilities and prevented Neogenix from obtaining an audit opinion on the company's financial statements. Ultimately, this uncertainty restricted Neogenix's ability to raise additional capital and the company declared bankruptcy in July 2012.

Conclusion

It is not uncommon for businesses to employ financial intermediaries, such as business brokers, "finders," and other types of consultants, to assist them in facilitating mergers and acquisitions, financing transactions, and other capital raising activities. Although many of the relevant statutes and rules have been in place for many years, their application to various types of financial intermediaries has recently captured the attention of the regulators. And, while the new developments in this area signify a willingness on the part of regulators to work towards more creative real-world solutions, they currently provide only limited relief. Moreover, although enforcement actions in this area may result in substantial fines and reputational damage, the long-term consequences of utilizing unregistered intermediaries can have even greater financial impact, such as, unwittingly providing rescission rights to investors. Accordingly, company executives and fund managers should continue to take care in their arrangements with financial intermediaries and with their own employees to ensure that all such persons are either properly registered or exempt from registration as broker-dealers.

ENDNOTES

* Stephen P. Wink is a member of the firm's Corporate Department and of the Capital Markets, Financial Regulatory, Investment Funds and Mergers & Acquisitions Practices. His practice focuses on advising a wide range of market players including investment banks, hedge funds, private equity firms, exchanges, alternative trading platforms, transfer agents and other financial institutions on matters involving the regulation

of broker-dealers and investment advisors, market regulation, and compliance and enforcement matters.

**Dana Fleischman is a member of the Corporate Department and the Capital Markets and Financial Regulatory Practices, as well as a member of the firm's Financial Institutions Group. Ms. Fleischman's practice focuses on matters involving the regulation of broker-dealers and securities markets, including in connection with public and private offerings, mergers and acquisitions and cross-border transactions, and assists U.S. and non-U.S. financial institutions in connection with registration issues, regulatory inquiries and internal investigations.

***Brett M. Ackerman is a member of the firm's Financial Institutions Group.

The information contained in this article is current as of March 28, 2014.

1 Although this article focuses on the broker-dealer registration requirements of the Exchange Act, we note that broker-dealer registration is also required under the various state securities or "blue sky" laws.

2 *See* Sections 3(a)(4) and 3(a)(5) of the Exchange Act. It is common to refer to a person that is a broker and/or dealer as a "broker-dealer."

3 *See, e.g.*, MuniAuction Inc., SEC No-Action Letter (available March 13, 2000); BondGlobe, Inc., SEC No-Action Letter (available February 6, 2001).

4 *See, e.g.*, Continental Grain Company, SEC No-Action Letter (available November 6, 1987); Fairfield Trading Corp., SEC No-Action Letter (available January 10, 1988); Acqua Wellington North American Equities Fund, Ltd., SEC No-Action Letter (available July 11, 2001).

5 *See, e.g.,* Herbruck, Alder & Co., SEC No-Action Letter (available June 4, 2002)

6 *See SEC v. Kramer*, 778 F. Supp. 2nd 1320 (M.D. Fla. 2011); *see also SEC v. Benger*, in the U.S. District Court for the Northern District of Illinois, No. 09 C 676, Memorandum Opinion and Order (Mar. 28, 2013) (rejecting the SEC's argument that anyone who facilitates any transaction in securities through conduct in the United States must register as a broker under Section 15(a) of the Exchange Act, even if the transaction did not involve the domestic sale of stock); *but cf.* In re Ambit Capital Pvt. Ltd., Order Instituting Administrative Proceedings, SEC Release No. 34-68295 (Nov. 27, 2012), In re Motilal Oswal Securities Limited, Order Instituting Administrative Proceedings, SEC Release No. 34-68296 (Nov. 27, 2012), In re JM Financial Institutional Securities Private Limited, Order Instituting Administrative Proceedings, SEC Release No. 34-68297 (Nov. 27, 2012), and In re Edelweiss Financial Services Limited, Order Instituting Administrative Proceedings, SEC Release No. 34-68298 (Nov. 27, 2012) (charging four financial services firms based in India for providing brokerage services to institutional investors in the United States without being registered with the SEC).

7 *See* Paul Anka, SEC No-Action Letter (available July 24, 1991).

8 *See* Record of Proceedings of 2008 Annual SEC Government-Business Forum on Small Business Capital Formation (Nov. 20, 2008).

9 *See* Country Business, Inc., SEC No-Action Letter (available November 8, 2006).

10 *See* SEC No-Action Letter, (available January 31, 2014) [Revised February, 4, 2014].

11 *See* AngelList LLC and AngelList Advisors LLC, Sec No-Action Letter (available March 28, 2013).

12 *See* FundersClub Inc. and FundersClub Management LLC, SEC No-Action Letter (available March 26, 2013).

13 *See* David W. Blass, A Few Observations in the Private Fund Space (April 5, 2013), available at: http://www.sec.gov/news/speech/2013/spch-040513dwg.htm

14 See Financial Industry Regulatory Authority Regulatory Notice 14-09, Rules for Limited Corporate Finance Brokers (February 2014), available at: http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/industry/p448158.pdf

15 *See* Report and Recommendations of the ABA Section of Business Law Task Force on Private Placement Broker-Dealers (June 7, 2005).

16 *See* the M&A No-Action Letter, *supra* note 1, at 2.

17 *See id.*

18 *See id.* at n. 1.

19 *See id.* at 2-3.

20 *See id.* at 3.

21 *See id.* at 2.

22 *See id.* at 2-3.

23 *See* M&A No-Action Letter, *supra* note 1, at 2.

24 *See* Blass Speech, *supra* note 4.

25 *See id.*

26 *See id.*

27 *See id;* 17 C.F.R. 240.3a4-1 (defining "associated person" as any natural person who is a partner, officer, director, or employee of: the issuer; a corporate general partner of a limited partnership that is the issuer; a company or partnership that controls, is controlled by, or is under common control with, the issuer; or an investment adviser registered under the Investment Advisers Act of 1940 to an investment company registered under the Investment Company Act of 1940 which is the issuer).

28 *See* 17 C.F.R. 240.3a4-1(a)(ii).

29 *See* Proposed Rules, *supra* note 5.

30 *See id.*

31 *See id.*

32 *See* Proposed Rule 116(b). If an existing firm is already approved to engage in the activities of an LCFB, and the firm does not intend to change its existing ownership, control or business operations, it would not be required to file either a New Member Application or a Change in Membership Application. Instead, such a firm would be required to file a request to amend its membership agreement or obtain a membership agreement (if none exists currently) to provide that: (i) the firm's activities will be limited to those permitted for an LCFB under LCFB Rule 016(g), and (ii) the firm agrees to comply with the LCFB Rules.

33 *See* Proposed Rule 121-124.

34 *See* 15 U.S.C. 80a-3(c)(7).

35 In re William M. Stephens, Order Instituting Administrative and Cease-and-Desist Proceedings, SEC Release No. 34-69090 (Mar. 8, 2013) (the Stephens Order). Stephens consented to the issuance of the order without admitting or denying the findings in the order; In re Ranieri Partners LLC and Donald W. Phillips, Order Instituting Administrative and Cease-and-Desist Proceedings, SEC Release No. 34-69091 (Mar. 8, 2013) (the Phillips Order). Phillips and Ranieri Partners consented to the issuance of the order without admitting or denying the findings in the order.

36 *See* the Phillips Order at 3.

37 *See id.*

38 *See id.*. In November 2002, the SEC had entered an order, based on an offer of settlement by Stephens, finding that Stephens violated certain provisions of the federal securities laws in connection with the investment of pension fund assets. At that time, Stephens agreed to a $25,000 civil penalty and to be barred from association with any investment adviser, with the right to reapply after two years (which Stephens did not do). Stephens' disciplinary history may have been an aggravating factor in this action.

39 *See id.*

40 *See id.* at 6.

41 *See* the Stephens Order at 6.

42 *See* the Phillips Order at 6.

43 *See id.*

44 *See* the Stephens Order at 6-7. The SEC waived those monetary penalties based on Stephens' sworn statement of his inability to pay disgorgement plus prejudgment interest or a civil penalty.

45 *See* the Phillips Order at 7.

46 *See id.* at 7-8.

47 *See* Neogenix Letter to Shareholders (available Nov. 23, 2011).

This article is reprinted with permission from *Practical Compliance and Risk Management for the Securities Industry,* a professional journal published by Wolters Kluwer Financial Services, Inc. This article may not be further re-published without permission from Wolters Kluwer Financial Services, Inc. For more information on this journal or to order a subscription to *Practical Compliance and Risk Management for the Securities Industry,* go to **pcrmj.com** or call **866-220-0297**