

Corporate Finance and Securities Law Update

6/5/2014

M&A Brokers: Don't Forget State Laws

On January 31, 2014, the Staff of the Securities and Exchange Commission (the "SEC") granted no-action relief permitting certain business brokers to facilitate the sale of privately-held companies and receive transaction-based compensation without registering as a broker-dealer under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). In the letter, the term "M&A Broker" is specifically defined as 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" through the purchase, sale, exchange, issuance, repurchase, or redemption of, or a business combination involving, securities or assets of the company, to a buyer that will actively operate the company or the business conducted with the assets of the company. In general, a "privately-held company," for purposes of the letter, is any non-SEC reporting company.

The Staff's position specifically permits the M&A Broker to advertise the privately-held company for sale; assess the value of any securities being sold; participate in negotiations for the transaction; advise the buyer and seller to issue securities; and, most importantly, receive transaction-based compensation. But there are a number of applicable conditions, including, among others:

- The buyer, individually or as part of a group, must as a result of the transaction obtain control of the acquired company. The requisite control will exist if the buyer has the power to direct the management or policies of the company, and control will be presumed if, upon completion of the transaction, the buyer has the right or power to vote, sell or direct the sale of 25 percent or more of a class of voting securities, or, in the case of a partnership or LLC, the right to receive upon dissolution or has contributed 25 percent or more of the capital.
- After the transaction, the buyer, individually or as part of a group, must actively operate the acquired company with the assets of the company. A transaction will not qualify if it results in the transfer of interests to a passive buyer. The letter provides that a buyer could 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.

- The transaction may not involve a public offering, and must be conducted in compliance with an applicable registration exemption.
- The M&A Broker (and, if an entity, its officers, directors and employees) may not be barred or suspended from association with a broker-dealer.

There has been significant commentary since the issuance of the letter regarding the permissible activities and conditions outlined above, but it is important to remember that the relief applies only to federal broker-dealer registration requirements under the Exchange Act. M&A Brokers must still comply with any applicable registration requirements under state laws. State law exemptions may be available, but that will not always be the case. The following addresses relevant state law considerations in Oregon, Washington and Alaska for M&A Brokers.

Oregon

In Oregon, the definition of “broker-dealer” does not include a person effecting sales in connection with a transaction exempt under the Oregon Securities Law. See ORS 59.015(1)(d). It may be possible to structure a transaction involving an M&A Broker to comply with ORS 59.035(2), which exempts an isolated nonissuer transaction, or ORS 59.035(5), which exempts any transaction by an offeror with an “accredited investor” (as such term is defined in the Oregon statute), but only if there is no public advertising or general solicitation in connection with the transaction. Reliance on ORS 59.035(12), relating to limited sales in Oregon, likely will not work for M&A Brokers because that exemption is conditioned on no commission or remuneration being paid in connection with the transaction.

Washington

In Washington, transactions set forth in RCW 21.20.320 are exempt from RCW 21.20.040 through RCW 21.20.300 and RCW 21.20.327 (except as otherwise provided), which provisions include the broker-dealer registration requirements under Washington law. It may be possible to structure a transaction involving an M&A Broker to comply with RCW 21.20.320(1), which exempts sales not involving a public offering, or another available exemption. However, it is important to note that the Division of Securities of the Washington Department of Financial Institutions may conclude that RCW 21.20.320(1) is available only in connection with sales by the company to be acquired, and not in connection with sales by a controlling owner or other affiliate of the company to be acquired.

Alaska

In Alaska, there appears to be no relevant exclusion or exemption available for M&A Brokers. Accordingly, an M&A Broker transacting business in Alaska may need to register as a broker-dealer with the Division of Banking and Securities of the Alaska Department of Commerce, Community, and Economic Development. However, it may be possible for M&A Brokers to receive formal or informal relief from the registration requirements based on the specific facts and circumstances of the intended corporate transaction to be completed.

As noted above, state law exemptions or relief may be available for M&A Brokers operating in Oregon, Washington and Alaska, but it will be important to carefully consider in advance what actions will be taken by brokers to ensure compliance with the securities law in such states. Moreover, the securities law of any other state in which the M&A Broker proposes to operate will need to be considered in advance of any activities to determine if there is an exemption or relief available, or if registration is required, in such other state.

For more information, please contact the Corporate Finance and Securities Practice Group at Lane Powell: lppc@lanepowell.com

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