Securities Intermediaries

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Clients often ask business attorneys how to obtain money to capitalize a new or expanding business and they are often approached by purported fundraisers who claim to be able to do so, often with upfront fees. Business attorneys should have some understanding as the legalities of such roles.

Securities intermediaries generally fit into one of the following buckets:

1) Registered broker-dealers – FINRA members
2) Exempt brokers
3) Finders – Registered with the Texas State Securities Board
4) Lead Brokers

FINRA Members

In 1938, the Maloney Act amended the Securities Exchange Act of 1934 (the "Exchange Act") to provide that the U.S. Securities and Exchange Commission (the "SEC") may delegate its licensing authority to "national securities associations."[2] The only current "national securities association" today is the Financial Industry Regulatory Authority or "FINRA." Today all federally registered broker-dealers are FINRA members. FINRA has the authority to issue rules approved by the SEC pursuant to the Exchange Act that have the full force of law applicable to FINRA members and their associated persons. This means that when FINRA members raise money for an issuer in any securities offering they must comply with a panoply of FINRA and SEC rules and interpretations.

Important requirements to FINRA members, relating to private placements, are the obligation to conduct a "reasonable investigation" into an issuer, and a variety of obligations to customers pursuant to SEC Regulation Best Interest[3] and the FINRA

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[2] 15 U.S.C. §78o-3.
[3] 17 CFR §240.15*l*-1

suitability rule,[4] if the customer has less than $50 million in total assets.[5] FINRA examiners have been critical of FINRA members conducing their own due diligence and an industry has grown involving third party due diligence firms who issue due diligence reports to their broker-dealer clients, reports paid for by the issuer.[6] These third-party due diligence reports help FINRA members meet their "reasonable investigation" obligations. Issuers engaging with FINRA members should understand that they will have obligations and procedures that are non-negotiable. For example, any offering with a minimum offering amount must have an escrow account at a bank.[7] The issuer cannot use a law firm or title company to escrow funds in connection with a securities offering conducted by a FINRA member.

An issuer not using a FINRA member in a private securities transaction may lead to issues on the quality of services provided, as well as legal risks.

Securities and Exchange Commission and Securities Exchange Act of 1934

Exchange Act Section 15(a) requires the registration of securities brokers and dealers with the SEC. That section states:

> It shall be unlawful for any broker or dealer which is either a person other than a natural person or a natural person not associated with a broker or dealer which is a person other than a natural person (other than such a broker or dealer whose business is exclusively intrastate and who does not make use of any facility of a national securities exchange) to make use of the mails or any means or instrumentality of interstate commerce to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) unless such broker or dealer is registered in accordance with subsection (b) of this section. [8]

Section 15(a)(1) disallows "any broker or dealer which is . . . a natural person not associated with a broker or dealer . . . to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security . . . unless such broker or dealer is registered [with the Commission]."[9] This registration exemption for persons associated

[4] FINRA Rule 2111; FINRA NTM 10-22.
[5] FINRA Rule 4512(c).
[6] Due diligence report providers include: 1) Buttonwood Due Diligence; 2) Mick Law P.C.; 3) Factright; and 4) Snyder Kearney LLC.
[7] 17 CFR §§240.10b-9; 240.15(c)(2)(4).
[8] 15 U.S.C. §78o.
[9] 15 U.S.C. §78o(a)(1).

with a broker-dealer "applies only if the person is acting within the 'scope' of his or her association with the member firm."[10]

The Exchange Act defines "broker" as "any person engaged in the business of effecting transactions in securities for the account of others."[11] The terms "engaged in the business" and "effecting transactions" are not defined by statute and are subject to interpretations.

Courts evaluating whether person acted as a broker under the Exchange Act standard consider whether that person: (1) works as an employee of the issuer; (2) receives a commission rather than a salary; (3) sells or earlier sold the securities of another issuer; (4) participates in negotiations between the issuer and an investor; (5) provides either advice or a valuation as to the merit of an investment; and (6) actively (rather than passively) finds investors.[12] These factors are not exclusive and no particular number of them must be satisfied for a person to be a broker. However, some courts have held that "the most important factor in determining whether an individual or entity is a broker" is the "regularity of participation in securities transactions at key points in the chain of distribution." [13]

Exchange Act Section 15(a) also includes a carveout from the federal broker-dealer registration requirement for "other than such a broker or dealer whose business is exclusively intrastate and who does not make use of any facility of a national securities exchange." Thus, if a person does not engage in transactions involving exchange-listed securities and the issuer, investor and broker are all in Texas, then that person is not required to be registered as a broker or dealer with the SEC.

The SEC routinely takes enforcement actions against persons acting as unregistered brokers who violate Section 15(a) of the Exchange Act.[14] If the SEC Enforcement Division investigates an issuer offering fraud whose securities were distributed through unregistered brokers, the complaint will inevitably also include claims against unregistered brokers. In such cases, the SEC Enforcement Division will seek disgorgement of commissions and other compensation paid to the broker, penalties, and injunctive relief.

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[10] *Roth v. SEC*, 22 F.3d 1108, 1109 (D.C. Cir. 1994); *SEC v. Westhead*. 2024 U.S. Dist. Lexis 120605 *32 (September 13, 2024).

[11] 15 U.S.C. §78c(a)(4).

[12] *S.E.C. v. Kramer,* 778 F. Supp. 2d 1320, 1334 (M.D. Fla. 2011); *SEC v. Westhead*. 2024 U.S. Dist. Lexis 120605 *32 (September 13, 2024); see also *SEC v Steve Qi & Law Offices of Steve Qi & Associates*, 2018 U.S. Dist. Lexis 239178 **18-20, (U.S.D.C. Central District California 2018); *SEC v. Collyard*, 861 F.3d 760, 765-766 (8th Cir. 2016); *SEC v. George*, 426 F.3d 786,797 (6th Cir. 2005); *S.E.C. v. Kramer,* 778 F. Supp. 2d 1320, 1333-1335 (USDC MD Florida 2011).

[13] *S.E.C. v. Kramer,* 778 F. Supp. 2d 1320, 1334 (M.D. Fla. 2011) (quoting from *S.E.C. v. Bravata*, No. 09-12950, 2009 WL 2245649, *2 (E.D. Mich. 2009); *SEC v. Westhead*. 2024 U.S. Dist. Lexis 120605 *32 (September 13, 2024).

[14] 21 U.S.C. 78*u*(d).

A SEC-derived federal court injunction for a violation of Section 15(a) will result in a 5 year "bad actor" disqualification from participating in private offerings under SEC Rule 506(d)(1)(ii). Such a bad actor disqualification would bar that person from being involved in private securities transactions, no matter how tangentially. Any offering the bad actor touches would likely lose access to securities registration exemptions. For example, a Texas Securities Commission Order issued in 2019 included a Texas Securities Commissioner finding that a person owned a minority interest in the issuer. Then, a federal court entered an injunction against the minority owner nine days before the issuer commenced its securities offering and there was no finding that issuer management knew of this injunction. The Texas Securities Commissioner issued a final Cease and Desist Order saying that the injunction causes the issuer to violate the Texas Securities Act's securities registration requirements.[15]

The SEC has completely failed to articulate a safe harbor to delineate those who are required to be registered as brokers and dealers and those who are not. The SEC no-action letter process has not been helpful, and in recent years come down to whether there was transaction-based compensation or not.

For example, the famous singer and songwriter Paul Anka is an Ottawa, Canada native and hockey fan. The Ottawa Senators were a NHL expansion team starting play in 1992. In 1991, it needed capital. The SEC issued no-action letter relief in 1991 to Paul Anka that would allow him to be compensated for referring contacts as potential investors in the Senators. Mr. Anka, a well-known singer, musician, and songwriter, was not "engaged in the business" of effecting securities transactions.[16] He contracted to provide names to the Senators' general partner of those who might consider buying equity securities issued by the Senators. Under the agreement, Mr. Anka was not to conduct any sales activity and only the Senators officers and directors participated in negotiations with prospective investors referred by Mr. Anka. Mr. Anka was to receive a commission. This was a high-water mark in the SEC providing relief to unregistered brokers.

In contrast, almost 30 years later, in 2010, the SEC issued another letter, denying no-action relief to the Brumberg, Mackey & Wall, P.L.C. law firm ("BMW") in which BMW was to introduce an issuers to prospective investors, but not negotiate the prospective transaction. The SEC staff denied no-action. Transaction-based compensation was enough to deny relief.

> A person's receipt of transaction-based compensation in connection with these activities is a hallmark of broker-dealer activity. Accordingly, any person receiving transaction-based compensation in connection with another person's purchase or sale of securities

[15] Texas Securities Commissioner Order No. ENF-20-CDO-1789 Agreed Cease and Desist Order styled *In the Matter of Sourcerock Energy Phoenix Prospect LP et al.* (September 20, 2019).
[16] Paul Anka SEC no-action letter (July 24, 1991).

> typically must register as a broker-dealer or be an associated person of a registered broker-dealer.[17]

Thus, the SEC has not created a safe harbor through its no-action letter process.

In October 2020, the SEC, under Chair Jay Clayton, issued a rule proposal articulating a proposed safe harbor for the scope of Section 15(a)'s broker and dealer requirements.[18] But shortly thereafter the presidential administration changed, Chair Clayton's term ended, and Chair Gary Gensler's term began. Chair Gensler had different priorities. The rule proposal has not been considered since its 2020 proposal and I do not anticipate the SEC revisiting the rule proposal without a change in the presidential administration. Election day is two days after this CLE presentation, but this paper was written in September 2024. So, for now, we will anticipate no further action from the SEC on creating a broker-dealer registration safe harbor.

On December 29, 2022, President Biden signed H.R. 2617 from the 117th Congress – the Consolidated Appropriations Act of 2023. This Act included an exemption from Exchange Act § 15(a)'s broker-dealer registration requirements for Mergers and Acquisition brokers and dealers in Exchange Act § 15(b). This statute became effective on March 29, 2023.

First, the Exchange Act § 15(b) exemption is limited to transactions involving issuers who: (1) are privately-owned entities who do not have any class of securities registered under Exchange Act § 12 or are required to file periodic reports with the SEC; (2) have earnings before interest, taxes, depreciation and amortization of less than $25 million in the previous fiscal year; (3) have gross revenues of less than $250,000,000 in the previous fiscal year; and (4) are not a shell company, except for a company created solely for the purpose of changing the corporate domicile within the United States or solely for completing a business combination transaction as described in SEC Rule 165 (collectively "M&A Transaction).[19]

Second, the exempted person must act as a "M&A" broker, which means:

> any person associated with a broker, engaged in the business of effecting securities transactions solely in connection with the transfer of ownership of an eligible privately held company, regardless of whether the broker acts on behalf of a seller or buyer, through the purchase, sale, exchange, issuance, repurchase, or redemption of, or a business combination involving, securities

[17] SEC no-action letter denial, *Brumberg, Mackey & Wall, P.L.C.*, May 17, 2010.
[18] *Notice of Proposed Exemptive Order Granting Conditional Exemption from the Broker Registration Requirements of Section 15(a) of the Securities Exchange Act of 1934 for Certain Activities of Finders*, Release No. 34-90112, File No. S7-13-20 (October 7, 2020).
[19] Securities Exchange Act §15(b)(13).

or assets of the eligible privately held company, if the broker reasonably believes that—

(I) upon consummation of the transaction, any person acquiring securities or assets of the eligible privately held company, acting alone or in concert—

(a) will control the eligible privately held company or the business conducted with the assets of the eligible privately held company; and

(b) directly or indirectly, will be active in the management of the eligible privately held company or the business conducted with the assets of the eligible privately held company, including without limitation, for example, by--

(i) electing executive officers;

(ii) approving the annual budget;

(iii) serving as an executive or other executive manager; or

(iv) carrying out such other activities as the Commission may, by rule, determine to be in the public interest; and

(II) if any person is offered securities in exchange for securities or assets of the eligible privately held company, such person will, prior to becoming legally bound to consummate the transaction, receive or have reasonable access to the most recent fiscal year-end financial statements of the issuer of the securities as customarily prepared by management of the issuer in the normal course of operations and, if the financial statements of the issuer are audited, reviewed, or compiled, any related statement by the independent accountant, a balance sheet dated not more than 120 days before the date of the offer, and information pertaining to the management, business, results of operations for the period covered by the foregoing financial statements, and material loss contingencies of the issuer.[20]

In connection with the definition of M&A Broker, "control" is specifically defined as:

Control. —The term 'control' means the power, directly or indirectly, to direct the management or policies of a company, whether through ownership of securities, by contract, or otherwise. There is a presumption of control if, upon completion of a transaction, the buyer or group of buyers—

(I) has the right to vote 25 percent or more of a class of voting securities or the power to sell or direct the sale of 25 percent or more of a class of voting securities; or

(II) 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.[21]

[20] Securities Exchange Act §15(b)(13)(E)(iv).

[21] Securities Exchange Act §15(b)(13)(E)(ii).

Third, Exchange Act § 15(b) provides that a person who fulfills the above-stated definition of "M&A Broker" shall be exempt from being required to register as a broker under registration, as long as the broker or dealer does not engage in any of the following activities in connection with the M&A Transaction:

(i) Directly or indirectly, in connection with the transfer of ownership of an eligible privately held company, receives, holds, transmits, or has custody of the funds or securities to be exchanged by the parties to the transaction.

(ii) Engages on behalf of an issuer in a public offering of any class of securities that is registered, or is required to be registered, with the Commission under Exchange Act § 12 or with respect to which the issuer files, or is required to file, periodic information, documents, and reports under subsection (d).

(iii) Engages on behalf of any party in a transaction involving a shell company, other than a business combination related shell company.

(iv) Directly, or indirectly through any of its affiliates, provides financing related to the transfer of ownership of an eligible privately held company.

(v) Assists any party to obtain financing from an unaffiliated third party without—

(I) complying with all other applicable laws in connection with such assistance, including, if applicable, Regulation T (12 C.F.R. 220 et seq.); and

(II) disclosing any compensation in writing to the party.

(vi) Represents both the buyer and the seller in the same transaction without providing clear written disclosure as to the parties the broker represents and obtaining written consent from both parties to the joint representation.

(vii) Facilitates a transaction with a group of buyers formed with the assistance of the M&A broker to acquire the eligible privately held company.

(viii) Engages in a transaction involving the transfer of ownership of an eligible privately held company to a passive buyer or group of passive buyers.

(ix) Binds a party to a transfer of ownership of an eligible privately held company.[22]

Finally, the majority of relevant Exchange Act cases hold that Section 15(a)[23] creates no private cause of action. Those cases include:

1. *Asch v. Philips, Appel & Walden, Inc*., 867 F.2d 776, 777 (2nd Cir. 1989);
2. *SEC v. Seaboard Corp., Admiralty Fund v. Hugh Johnson & Co.*, 677 F. 2d 1301, 1313–14 (9th Cir. 1982);
3. *Brannan v. Eisenstein,* 804 F. 2d 1041, 1041 n.1 (8th Cir. 1986);
4. *Bull v. Am. Bank & Trust Co. of Pa.*, 641 F.Supp. 62, 65 (E.D. Pa. 1986);
5. *Sheldon v. Vermonty*, 204 F.R.D. 679, 684–85 (D. Kan. 2001);
6. *Bamert v. Pulte Home Corp*., 202 U.S. DIST. LEXIS 112688, at *18 (M.D. Fla. 2012);
7. *Olsen v. Paine, Webber, Jackson & Curtis, Inc.*, 623 F.Supp. 17, 18 (M.D. Fla. 1985);
8. *Kidder Peabody & Co. Inc. v. Unigestion Int'l, Ltd*., 903 F. Supp. 479, 493–95 (S.D.N.Y. 1995).

However, two cases held that there was a private cause of action under §15(a):

1. *Eastside Church of Christ v. National Plan, Inc*., 391 F.2d 357, 361-62 (5th Cir. 1968);
2. *Landegger v. Cohen*, F. Supp. 3d 1278 (D. Colo. 2013).

Of note, the Fifth Circuit precedent (*Eastside Church of Christ*) dates from 1968 before the Supreme Court decided *Cort v. Ash*, 422 U.S. 66 (1975) in which it provided a new analytical framework for determining whether a statute has an implied private cause of action. That analytical framework is:

> In determining whether a private remedy is implicit in a statute not expressly providing one, several factors are relevant. First, is the plaintiff "one of the class for whose *especial* benefit the statute was enacted, -- that is, does the statute create a federal right in favor of the plaintiff? Second, is there any indication of legislative intent, explicit or implicit, either to create such a remedy or to deny one? Third, is it consistent with the underlying purposes of the legislative scheme to imply such a remedy for the plaintiff? And finally, is the cause of action one traditionally relegated to state law, in an area basically the concern of the States, so that it would be inappropriate to infer a cause of action based solely on federal law?[24]

[22] Securities Exchange Act §15(b)(13)(B).
[23] 15 U.S.C. §78*o*(a).
[24] *Cort v. Ash*, 422 U.S. 66, 78 (1975) (citations omitted).

Texas Securities Act

The Texas Securities Act ("TSA") has incredibly broad definitions of "broker" and "dealer." Importantly, unlike the Exchange Act, there is no requirement that the broker or dealer be "engaged in the business." One transaction is enough. Moreover, the TSA has an issuer-dealer provision.

> **Sec. 4001.054. Broker.** "Broker" means "dealer" as defined in this title.[25]
>
> **Sec. 4001.056. Dealer.**
> (a) "Dealer" includes:
> (1) a person or company, other than an agent, who for all or part of the person's or company's time engages in this state, directly or through an agent, in selling, offering for sale or delivery, soliciting subscriptions to or orders for, undertaking to dispose of, or inviting offers for any security; and
> (2) a person or company who deals in any other manner in any security in this state.
> (b) Except as provided by Subsection (c), an issuer, other than a registered dealer, who directly or through any person or company, other than a registered dealer, offers for sale, sells, or makes sales of the issuer's own securities is deemed a dealer and shall comply with this title.
> (c) An issuer is not deemed a dealer under Subsection (b) if:
> (1) the issuer sells or offers for sale securities to a registered dealer or only by or through a registered dealer acting as fiscal agent for the issuer; or
> (2) the transaction is exempt as provided by Subchapter A, Chapter 4005.[26]

The TSA also has a very broad definition of "sale, including "any act by which a sale is made":"

> **Sec. 4001.067. Sale; Offer for Sale; Sell.**[21]
> (a) "Sale," "offer for sale," and "sell" include every disposition or attempted disposition of a security for value.
> (b) "Sale" means and includes:
> (1) a contract or agreement in which a security is sold, traded, or exchanged for money, property, or another thing of value; or
> (2) a transfer of or agreement to transfer a security, in trust or otherwise.

[25] Tex. Gov't Code §4001.054.
[26] Tex. Gov't Code §4001.056.

(c) "Sale" or "offer for sale" includes a subscription, an option for sale, a solicitation of sale, a solicitation of an offer to buy, an attempt to sell, or an offer to sell, directly or by an agent, by a circular, letter, or advertisement or otherwise, including the deposit in any manner in the United States mail within this state of a circular, letter, or other advertising matter.
(d) ***"Sell" means any act by which a sale is made***.
(e) A security given or delivered with or as a bonus on account of a purchase of securities or other thing of value is conclusively presumed to:
  (1) constitute a part of the subject of the purchase; and
  (2) have been sold for value.
(f) The sale of a security under conditions that entitle the purchaser or subsequent holder to exchange the security for another security or to purchase another security is not deemed a sale or offer for sale of the other security.
(g) This section does not limit the meaning of the terms "sale," "offer for sale," or "sell" as used by or accepted in courts. (emphasis added)

This broad definition means that the TSA has no limitations such as "engaged in the business."

The TSA can be enforced by the Texas Securities Commissioner and the State of Texas with administrative,[27] civil,[28] and criminal (felony in the third degree) [29] remedies all applicable to parties acting as an unregistered broker or dealer.

The TSA has private causes of action against unregistered brokers and dealers who represent the seller of the securities, but not against those who represent the buyer.[30] Further, unregistered brokers may not bring actions relating to unpaid commissions unless such broker proves compliance with an exemption from the broker-dealer registration requirements.[31] Any party claiming an exemption from the broker-dealer registration requirements has the burden of proof to prove such exemption.[32] To prove the lack of registration, attorneys may contact the Texas State Securities Board ("TSSB" or the "Board") to obtain a sealed and signed certificate of the absence of a public record.[33]

[27] Tex. Gov't Code §§4007.101, 4007.102, 4007.103, 4007.104, 4007.105, 4007.106, and 4007.108.
[28] Tex. Gov't Code §§4007.151 and 4007.152.
[29] Tex. Gov't Code §§4007.201(b) and (c).
[30] Tex. Gov't Code §4008.051(a).
[31] Tex. Gov't Code §§4008.001 and 4008.003; *see e.g.* 7 Tex. Admin. Code §109.14(d) (listing a common broker-dealer registration exemptions relating to oil and gas interests and industry-related purchases) *and* 7 Tex. Admin. Code § 139.27 (listing a common broker deal registration exemption for certain mergers and acquisitions broker-dealers).
[32] Tex. Gov't Code §4001.153.
[33] Tex. R. Evid. 902.

Most registered broker firms and persons licensed with the Texas Securities Commissioner are FINRA-registered firms and their associated persons. In addition, there are three further registrations and exemptions worth discussing: the finder registration, the mergers and acquisition broker-dealer exemption, and the landman exemption for oil and gas industry purchasers.

Finder Registration

The Texas State Securities Board adopted a limited broker-dealer registration for "finders," who are individuals who refer accredited investors,[34] whether individual or institutional, to an investment, and are compensated if their referral makes a purchase.[35] But the finders may not be involved in negotiating the sale, advising about the investment, or performing due diligence.[36] This finder broker-dealer registration is available only to individuals, and dispenses with the exam requirement and the need to affiliate with a registered broker-dealer.[37] It requires that finders maintain certain records and not commingle the finder-related records with other records.[38] It also requires that finders disclose in writing that the issuer pays them and their potential conflicts of interest, and provide a statement that the finder can neither recommend, nor advise, the accredited

[34] The Texas Finder Rule apparently applies to all different definitions of "accredited investor" for non-natural persons under the Texas State Securities Board Rules. Those definitions are: (1) an accredited investor defined by reference to SEC Regulation D, see 7 Tex. Admin. Code §§109.4(b)(1), 109.5(b)(1), 109.6(b)(1), and 139.19; (2) any bank as defined in the Securities Act of 1933, §3(a)(2), whether acting in its individual or fiduciary capacity, see 7 Tex. Admin. Code §109.13(l)(11)(A); (3) insurance company as defined in the Securities Act of 1933, §2(13), see 7 Tex. Admin. Code §109.13(l)(11)(A); (4) investment company registered under the Investment Company Act of 1940 or a business development company as defined in that Act, §2(a)(48), see 7 Tex. Admin. Code §109.13(l)(11)(A); (5) small business investment company licensed by the U.S. Small Business Administration under the Small Business Investment Act of 1958, §301(c) or (d), see 7 Tex. Admin. Code §109.13(l)(11)(A); (6) employee benefit plan within the meaning of the Employee Retirement Income Security Act of 1974, Title I, if the investment decision is made by a plan fiduciary, as defined in such Act, §3(21), which is either a bank, insurance company, or investment adviser registered under the Investment Advisers Act of 1940, or if the employee benefit plan has total assets in excess of $5 million, see 7 Tex. Admin. Code §109.13(l)(11)(A); (7) any private business development company as defined in the Investment Advisers Act of 1940, §202(a)(22), see 7 Tex. Admin. Code §109.13(l)(11)(B); (8) any organization described in the Internal Revenue Code, §501(c)(3), with total assets in excess of $5 million, see 7 Tex. Admin. Code §109.13(l)(11)(C); (9) any (non-natural person) director, executive officer, or general partner of the issuer of the securities being offered or sold, or any director, executive officer, or general partner of a general partner of that issuer, see 7 Tex. Admin. Code §109.13(l)(11)(D); (10) any (non-natural) person who purchases at least $150,000 of the securities being offered, where the purchaser's total purchase price does not exceed 20% of the purchaser's net worth at the time of sale, or joint net worth with that person's spouse, for one or any combination of the following: (i) cash; (ii) securities for which market quotations are readily available; (iii) any unconditional obligation to pay cash or securities for which market quotations are readily available which obligation is to be discharged within five years of the sale of securities to the purchaser; or (iv) the cancellation of any indebtedness owed by the issuer to the purchaser, see 7 Tex. Admin. Code §109.13(l)(11)(E); and (11) any entity in which all of the equity owners are accredited investors, see 7 Tex. Admin. Code §109.13(l)(11)(F).

[35] 7 Tex. Admin. Code §§115.1(a)(9) and 115.11.

[36] 7 Tex. Admin. Code §115.11(a).

[37] 7 Tex. Admin. Code §115.1(a)(9).

[38] 7 Tex. Admin. Code §115.11(c).

investor about the investment.[39] Such disclosure should include a statement that the finder's compensation relies on making the sale, and the finder has incentives to hope the transaction closes.[40]

Finder registration protects finders against unenforceable commission contracts and penalties for non-registration, including criminal penalties. But the Texas Finder Rule imposes some burdens. First, finders must complete an application and pay a fee (currently $75) to the TSSB.[41] No exam is required.[42] A link to the application form, "Form BD," can be found on the Board's website (www.ssb.state.tx.us) under "Forms and Fees." Board examiners will review the application for possibly disqualifying events such as criminal fraud convictions, securities industry bars, and court-issued securities fraud injunctions, and then grant or deny registration.[43] Denials would likely be rare and may be appealed to the State Office of Administrative Hearings for review.[44]

The Texas Finder Rule limits the finder to giving the issuer only the prospective accredited investor's contact information[45] and only providing the prospective accredited investor the following information:

1) the name, address, and telephone number of the issuer of the securities;
2) the name, a brief description, and price (if known) of any security to be issued;
3) a brief description of the business of the issuer in 25 words or less;
4) the type, number, and aggregate amount of securities being offered; and/or
5) the name, address, and telephone number of the person to contact for additional information.[46]

The Texas Finder Rule requires that certain records relating to completed transactions be maintained for five (5) years,[47] and records more than two (2) years old may be archived.[48] The finder is also barred from commingling the finder records with records from the finder's other businesses.[49] The rule requires finders to keep:

1) compensation records for acting as finder, including the name of the payor, date of payment, name of issuer, and the name of the accredited investor;
2) copies of the information provided by the finder to the prospective accredited

[39] 7 Tex. Admin. Code §115.11(b).
[40] 7 Tex. Admin. Code §115.11(b).
[41] Tex. Gov't Code §4006.001; *see* Texas State Securities Board, *Dealer Checksheets for Registration*, https://ssb.texas.gov/securities-professionals/dealer-adviser-registration/registration-dealers/dealer-checksheets.
[42] 7 Tex. Admin. Code §115.3(c)(2)(E).
[43] 7 Tex. Admin. Code §104.5; *see* Tex. Gov't Code §4007.105.
[44] 7 Tex. Admin. Code §§ 105.1-105.23; Tex. Gov't Code §§2001.054, 2001.058 and 2003.021.
[45] 7 Tex. Admin. Code §115.11(c)(2).
[46] 7 Tex. Admin. Code §115.11(c)(1).
[47] 7 Tex. Admin. Code §§115.11(d)(2) and 115.11(d)(3).
[48] 7 Tex. Admin. Code §115.11(d)(5).
[49] 7 Tex. Admin. Code §115.11(d)(6).

investors;
3) agreements between the finder and the accredited investor and between the finder and the issuer;
4) contact lists of prospective accredited investors and issuers; and
5) correspondence with accredited investors and issuers, including e-mail.[50]

Finally, the Texas Finder Rule requires finders provide copies of these records to the TSSB staff upon request,[51] including allowing TSSB examiners to inspect records.[52]

Mergers and Acquisitions Broker-Dealer Exemption

Under the Merger and Acquisition Broker-Dealer exemption under Texas State Securities Board Rule 139.27 the TSSB exempted persons from the TSA's broker-dealer registration requirements for services related to a "Qualifying M&A Transactions" involving "Privately-Held Companies." Privately-Held Companies are business entities that are neither SEC-reporting issuers nor shell companies. Qualifying M&A Transactions are:

1) a transfer of ownership and control of a Privately-Held Company to a buyer through the purchase, sale, exchange, issuance, repurchase, or redemption of securities, or a business combination involving securities or assets of the company;

2) Upon completion of the transaction, the buyer or group of buyers must actively operate the company or the business conducted with the assets of the company;

3) No Qualifying M&A Transaction can involve a public offering of securities. Any offering or sale of securities will be conducted in compliance with an applicable exemption from registration under the Texas Securities Act;

4) No party to any Qualifying M&A Transaction can be a shell company, other than a shell company formed by the buyer for the purposes of closing the transaction; and

5) The buyer, or group of buyers, in any Qualifying M&A Transaction must, upon completion of the transaction, control the company. A buyer, or group of buyers collectively, would have the necessary control if it has 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% or more of a class of voting securities; has the power to sell or direct the sale of 25% or more of a class of voting securities; or in

[50] 7 Tex. Admin. Code §115.11(d)(3).
[51] 7 Tex. Admin. Code §115.11(d)(7).
[52] 7 Tex. Admin. Code §115.7.

the case of a partnership or limited liability company, has the right to receive upon dissolution or has contributed 25% or more of the capital.[53]

Landman Exemption

Lastly, the TSSB Rule 109.14(d) contains the landman exemption. The Rule provides for broker-dealer and securities registration exemptions in brokered transaction of "interest in or under an oil, gas, or mining lease, fee, or title, or payments out of production in or under such leases, fees, or titles or contracts relating thereto" when the purchaser:

(A) is engaged in the business of exploring for or producing oil, gas, or other minerals as an ongoing business or is engaged in the practice of a profession, or discipline, which is directly related to the exploration for, production of, refining of, or marketing of oil, gas, or other minerals such as the interest being sold; or
(B) is a landman, drilling company, well service company, production company, refining company, geologist, geophysicist, petroleum engineer, earth scientist; or
(C) is an executive officer of a company whose primary plan of business involves either subparagraphs (A) or (B) of this paragraph.[54]

Lead Brokers

Lead Brokers provide issuers leads to prospective investors, charging a per lead fee and not having any transaction-based compensation. Further, lead brokers do not communicate with prospective investors about the issuer's proposed investment. As such, lead brokers should be outside the definitions of broker or dealer.

[53] 7 Tex. Admin. Code §139.27.
[54] 7 Tex. Admin. Code §109.14(d)(1).