

SEC PROPOSAL FOR LIMITED EXEMPTION FROM BROKER-DEALER REGISTRATION

On October 7, 2020, the Securities and Exchange Commission (the “SEC”) proposed a limited, conditional exemption from the broker registration requirements of Section 15(a) of the Securities Exchange Act of 1934 (the “Exchange Act”) for finders in connection with the sale of securities in private offerings by issuers. If adopted, the proposed exemption would allow finders to connect issuers with potential accredited investors and receive transaction-based compensation in exchange for such services without the need to register as broker-dealer.

The proposed exemption separates finders into two distinct categories, largely based on the nature and extent of interactions the finders will have with potential investors, as follows:

Tier I Finders:

- May provide contact information of potential investors to issuers in connection with a single capital-raising transaction by a single issuer in a 12-month period
- May not have any contact with a potential investor about the issuer or the offering

Tier II Finders:

- May identify, screen, and contact potential investors
- May distribute issuer offering materials to potential investors
- May discuss issuer information included in offering materials
- May arrange or participate in meetings with the issuer and potential investor

Because Tier II Finders have a greater scope of permissible activities than Tier I Finders, there are additional, heightened disclosure requirements for Tier II Finders in the proposed exemption related to the finders’ role and compensation. If adopted, a Tier II Finder will be required to obtain a written acknowledgement of those disclosures from the potential investor prior to or at the time of solicitation.

The proposed exemption would limit the scope of activities of both Tier I Finders and Tier II Finders to identifying, and in the case of Tier II Finders, contacting and connecting investors to issuers and distributing information to investors. The proposed exemption would not permit a finder to participate in the structuring or negotiating of terms of the transaction, prepare sales materials, provide advice on the valuations or merits of the transaction, or otherwise engage in due diligence activities.

In addition to the limitations outlined above, the proposed exemption would require a potential investor to be, to the reasonable belief of the finder, an “accredited investor.” In addition, the finder and the issuer must enter into a written agreement that includes both a description of services and the associated compensation. The finder must not be subject to a statutory disqualification and must not be an associated person of a broker-dealer. Finally, the issuer must not be subject to any reporting requirements under Section 13 or Section 15(d) of the Exchange Act and must be offering securities in reliance on an applicable exemption from registration.

The proposed exemption will be subject to a 30-day comment period once published in the Federal Register. If adopted, this exemption will be helpful in addressing ambiguities related to the status of a finder, particularly for those engaged in early-stage transactions where the issuer’s network may be limited.

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