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Client Alert: M&A Broker Exemption Takes Effect

A new law exempting certain “M&A brokers” from having to register with the SEC took effect on March 29. This will enable many boutique “investment banks” which only engage in transactions with eligible privately held companies to avoid burdensome regulations.

On December 29, 2022, President Biden signed into law new provisions contained in the Consolidated Appropriations Act, 2023 (H.R. 2617) [see pp. 1080-1084] which create a statutory exemption from Federal broker/dealer registration for certain “M&A brokers.”

M&A Broker

The Exemption defines an “M&A Broker” as a broker and any associated person that is engaged in the business of effecting securities transactions (whether sell-side or buy-side) solely in connection with the transfer of ownership of an “eligible privately held company” through the purchase, sale, exchange, issuance, repurchase or redemption of, or a business combination involving securities or assets of the eligible privately held company, if the broker reasonably believes that:

- Upon consummation of the transaction, any person acquiring securities or assets, acting alone or in concert (1) will control the eligible privately held company or the business conducted with the assets of the eligible privately held company (for example, by electing executive officers, approving the annual

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budget, or serving as an executive or other executive manager); and (2) 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.

- Any buyer, before becoming legally bound to consummate the transaction, has received or has reasonable access to various disclosure documents customarily prepared by company management, including, among others, the company's most recent fiscal year-end financial statements (which need not be audited), as well as information pertaining to the management, business, results of operations, and material loss contingencies of the issuer.
- An "eligible privately held company" is defined as a company that has, in the fiscal year ending immediately before the fiscal year in which the services of the M&A broker are initially engaged with respect to the transaction: (i) no class of securities registered or required to be registered under §12 of the Exchange Act and (ii) earnings before interest, taxes, depreciation, and amortization (EBITDA) of less than \$25 million and/or gross revenues of less than \$250 million. Those amounts will be adjusted for inflation five years after the date of enactment and every five years thereafter.

"Control" is defined as the power to, directly or indirectly, 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 has the right to vote, sell, or direct 25% or more of a class of voting securities or, in the case of a partnership or LLC, has contributed or has the right to receive upon dissolution 25% or more of the capital.



Scope of Exemption

To remain exempt, an M&A Broker cannot engage in any of the following activities:

- *Custody*: Directly or indirectly receiving, holding, transmitting, or having custody of funds or securities of the parties in connection with the transaction.
- *Public securities*: Engaging on behalf of an issuer in a public offering of any class of securities registered (or required to be registered) under §12 of the 1934 Act or for which the issuer files (or is required to file) periodic reports under §15(d) of 1934 Act,
- *Shell companies*: Engaging in a transaction involving a shell company, other than a “business combination related shell company” formed solely for purposes of the transaction,
- *Financing*: Providing financing to a party to the transaction directly or indirectly through any of its affiliates, or assisting any party to obtain financing from an unaffiliated third party without complying with all other applicable laws in connection with such assistance, including, if applicable, Regulation T; and disclosing any compensation in writing to the party.
- *Joint representation*: Representing both the buyer and the seller in the same transaction without providing written disclosure as to the parties represented and obtaining written consent from both parties to the joint representation.
- *Buying groups*: Assisting in the formation of a group of buyers to acquire the eligible privately held company.
- *Passive buyers*: Engaging in a transaction involving the transfer of ownership of an eligible privately held

company to a passive buyer or group of passive buyers.

- *Contracting authority*: Binding a party to a transfer of ownership of an eligible privately held company.

An M&A broker will be disqualified from taking advantage of the Exemption if the M&A broker (including any officer, director, member, manager, partner or employee associated with the broker) has been barred from association with a broker or dealer by the SEC, any state, or any self-regulatory organization or suspended from association with a broker or dealer. The M&A broker exemption only applies to Federal registration with the SEC, and does not preempt state broker registration laws or regulatory requirements. Therefore, although an M&A broker may be exempt from Federal registration, that M&A broker may still be required to register with one or more states due to activity in or with residents of that state. Approximately half of the states have similar conditional M&A broker registration exemptions or other regulatory relief available.

Action Items

Although the Exemption is self-executing and does not require any notice filing, M&A brokers should contact their NG&E attorney to (i) assist in analyzing and determining whether they are eligible to rely upon the Exemption, (ii) analyze applicable state regulatory laws, (iii) review and prepare documents to be used by the M&A broker, such as “M&A engagement letter agreements”, (iv) review M&A broker advertising or marketing, including websites, and (v) establish procedures designed to ensure ongoing compliance with the requirements of the Exemption.

Should you have any questions about this guidance or any other matters related to the M&A Broker Exemption



law, please contact Wesley Nissen, Michael Gray or your Neal Gerber Eisenberg attorney.

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