

June 2010

SECURITIES LAW ALERT

SEC STAFF DECLINES TO PERMIT A FINDER IN A SECURITIES OFFERING TO RECEIVE TRANSACTION-BASED COMPENSATION WITHOUT BEING REGISTERED AS A BROKER-DEALER

In May 2010, the staff (the "Staff") of the Division of Corporation Finance of the Securities and Exchange Commission ("SEC") declined to issue a No-Action Letter (Brumberg, Mackey & Weil, P.L. C., No Action Letter, May 17, 2010) that would have permitted a law firm to receive transaction-based compensation for referring investors to a company that was seeking to raise capital without the law firm being registered as a broker-dealer under Section 15(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). The proposed referral agreement provided that the law firm would receive a percentage of the amounts raised from investors referred to the company by the law firm.

Section 3(a)(4)(A) of the Exchange Act generally defines the term "broker" as any person engaged in the business of effecting transactions in securities for the account of others. Section 15(a)(1) of the Exchange Act generally provides that any broker effecting transactions in securities, or inducing or attempting to induce the purchase or sale of securities, must be registered with the SEC pursuant to Section 15(b) of the Exchange Act.

The Staff was not persuaded by the law firm's argument that the firm should not be required to be registered as a broker-dealer because it:

- would not engage in any negotiations whatsoever on behalf of the company and any investor;
- would not provide any investor with any information about the company which may be used as the basis for any negotiations for funding to be provided to the company;
- would not have any responsibility for, nor make any recommendations concerning, the terms, conditions, or provisions of any agreement between the company and any investor providing funding for the company; and
- would not provide any assistance to any investor or the company with respect to any transactions involving the financing of funds for the company.

The Staff indicated that the receipt of compensation directly tied to the purchase of the company's securities by investors introduced to the company by the law firm (i.e., transaction-based compensation) would give the law firm a "salesman's stake" in the proposed transactions and would create heightened incentive for the law firm to engage in sales efforts. According to the Staff, a person's receipt of transaction-based compensation in connection with these activities is a hallmark of broker-dealer activity. As a result, the Staff indicated that the law firm's proposed activities would require broker-dealer registration.

The Staff's position in this No-Action Letter illustrates the risk that an unregistered finder who receives transaction-based compensation in connection with a securities offering will be subject to liability for failing to register as a broker-dealer.

(Please see next page for more information.)

666 Fifth Avenue, 28th Floor • New York • NY 10103-0084
600 Old Country Road • Citibank Building • Garden City • NY 11530-2011
Court Plaza North • 25 Main Street, 6th Floor • Hackensack • NJ 07601-7015

212.977.9700 Tel • 212.262.5152 Fax
516.229.9400 Tel • 516.228.9612 Fax
201.487.3700 Tel • 201.646.1764 Fax

This is also a matter of concern for issuers of securities since hiring an unlicensed broker-dealer to effect a securities offering is a violation of federal and many state securities laws. It also results in a voidable transaction that gives the investor, buyer or seller, a right of rescission, effectively granting a put right to the investor or purchaser.

For additional information, the following is a link to the No-Action Letter:

<http://www.sec.gov/divisions/marketreg/mr-noaction/2010/brumbergmackey051710.pdf>

We are available to provide counsel and guidance concerning similar Securities Law issues, as well as others not discussed in this Alert. Please contact any of the attorneys named below.

Contact:	R. Brian Brodrick	212.841.0700	bbrodrick@phillipsnizer.com
	Elliot H. Lutzker	212.841.0707	elutzker@phillipsnizer.com
	Andrew E. Goldstein	212.841.0729	agoldstein@phillipsnizer.com

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