

Houston Business Journal - February 5, 2007

<http://houston.bizjournals.com/houston/stories/2007/02/05/focus1.html>

HOUSTON BUSINESS JOURNAL

BUSINESS PULSE SURVEY: [How do you think the state budget surplus should be spent?](#)

New rule clarifies when 'finders' can be keepers

chall@bizjourn

Houston Business Journal - February 2, 2007 by [Christine Hall](#) Houston Business Journal

Those in Texas acting as "finders" -- professionals who bring together potential investors and companies in need of investors -- may now have more in common with securities brokers than they thought.

The Texas State Securities Board recently passed a new rule to add a restricted dealer registration category for those who act solely as finders.

For years, finders were able to claim exemption from the rules set forth for brokers, but by adding the term to the new act, finders are now considered on similar terms as brokers.

The board defines a finder as an individual "who receives compensation solely for introducing accredited investors to a company issuing securities and/or introducing an issuer to accredited investors."

In addition, finders are prohibited from negotiating any terms of the investment and giving advice to parties regarding the positive and negative attributes of the investment.

Performing those activities is where many finders "find" themselves crossing the gray area into the realm of brokers, and one of the reasons the board enacted the rule, says Nelson Ebaugh, securities attorney for Zimmerman, Axelrad, Meyer, Stern & Wise PC.

"When finders do things only licensed brokers can do it becomes a big issue," he says. "While finders can assist in a limited capacity, once they perform any of the hallmark activities of a broker, they run the risk of being prosecuted as an unlicensed broker."

Ebaugh knows from experience -- he has consulted and represented finders in the past.

One of the ways he has seen finders get into trouble is by accepting a commission rather than a flat fee for their services.

For example, if a finder helps a biomedical company find an investor, the finder must negotiate a flat fee for his services.

"The problem comes in," Ebaugh says, "when the biomedical company tells the finder it will give him 6 percent of whatever money is raised."

Rules to abide by

Texas is the second state to register finders, following Michigan which has had the rule on its books since 1978.

The Michigan Uniform Securities Act added the term finder "in an attempt to cover business intermediaries who do not neatly fit the broker-dealer or investment adviser categories," according



David A. Farias/HBJ
Securities attorney Nelson
Ebaugh of Zimmerman,
Axelrad, Meyer, Stern &
Wise PC: 'When finders do
things only licensed brokers
can do it becomes a big
issue.'

[View Larger](#)

to the statute.

Like Michigan, Texas is requiring finders to disclose in writing that they are acting as a finder. Michigan further requires them to say by which method and the amount of payment, while Texas requires only that a finder disclose that they will be paid a compensation.

Meanwhile, the South Dakota Division of Securities is in the process of adopting an act, which will include a provision on finders, called the "South Dakota Franchise Investment Act of 2007." New rules went into effect in October.

While the new regulations may have finders hopping, it does help companies like The Woodlands-based MGL Consulting Corp., which provides registration and compliance services to broker/dealers, investment advisers and insurance companies.

Although MGL Consulting does not deal with finders, Daniel LeGaye, executive vice president and general counsel, says the new rules are a major step forward for a state.

"It gives my clients the means to legally pay a finder on a limited basis in Texas," he says. "I would have liked it to be broader, but this was a major move for the state."

While LeGaye says there will be an increase in activity as finders want to be registered, the rule does not help his clients, such as investment advisers, because they perform services like valuations and give advice.

Wide support

Although the new rule forces finders to be registered before they act as a finder, both licensed and unlicensed brokers are behind the new regulation.

Bryan Emerson, managing director of Starlight Capital Inc., says the regulation puts people on an even playing field.

"You are trusted with people's money, so you have a duty to protect the public," says Emerson, who is a licensed broker. "Now everyone must play by the same rules."

In a letter to California's Office of Law and Legislation in November, Emerson lobbied for the state to have a similar rule to Texas.

He expressed his views that investors should have access to a financial professional's background and regulatory dealings, as well as recommending that those who are registered should take part in continuing education courses.

"Too many unlicensed persons who compete in this space do not have the knowledge, skills or abilities to help their clients make informed decisions, which results in a waste of time, money and opportunity costs," he writes. "They don't consider 'suitability' in their recommendations, don't perform due diligence on any of the parties involved and don't establish escrow accounts or undertake other reasonable measures designed to protect all parties."

In addition, he says that unlicensed finders are taking advantage of their independence by not acting in the best interests of their clients.

Meanwhile, Marc Nathan, a principal at Bulldog Financial, says at one time he owned a company that was licensed, but decided to sell it when being registered was not worth the cost.

However, depending on the amount a company is looking for, the only option may be hiring those who are unlicensed.

"If you are a company looking for \$300,000 to \$1 million, you are only going to find unlicensed individuals," Nathan says. "Those who deal with more can't live on those kinds of fees and be licensed."

But, he adds, the new rule keeps things legitimate and puts a gap between what finders and licensed brokers could do.

Says Nathan: "Raising capital is not easy, and there are some bad people out there which is why we

have the regulation."

This article is for Paid Print Subscribers ONLY.

If you are already a Houston Business Journal subscriber please **create or sign into your bizjournals.com account to link your valid print subscription** and have access to the complete article.

Become a Print Subscriber



For immediate access to this article, as well as the most recent edition of Houston Business Journal online, become a print subscriber.

[Purchase a Print Subscription](#)

[Create a Bizjournals Account](#)

Already have an Account

Email Address:

Password:

[Forgot Your Password?](#)

[Contact the Editor](#)

[Need Assistance?](#)

[More Latest News →](#)

[Subscribe or renew online](#)

All contents of this site © American City Business Journals Inc. All rights reserved.