

# Jacobs Law Group News

Business Lawyers and Litigators

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## THE DANGER OF FINDERS FEES

### How Exploiting Your Contacts Can Result In Securities Law Violations

Finally after years of building up your contacts you have a real chance to make a windfall profit by introducing a friend looking to raise capital to other friends of yours who have capital to invest and/or money to loan. All you want is a reasonable fee to compensate you for the tremendous value you are giving to your friend by giving him access to your network. You figure that ten percent (10%) of the funds raised is reasonable and your friend agrees. As luck would have it, your friend raises \$5.0 MM from your contacts and calls you to set a date to celebrate with you and go out to dinner and of course give you a check for \$500,000.

Now what could be wrong with that? Well, it's unlawful and not only might you have to return it; you may have serious problems with the government.

According to the Pennsylvania Securities Commission, "Pennsylvania does not allow the payment of finder's fees for sales of securities to Pennsylvania residents". In *The Matter Of: Phymed Partners Inc.*, 2002 Pa. Sec. LEXIS 155 (Pa. Sec. 2002). Indeed, persons who attempt to obtain finders fees are deemed to be broker dealers under Pennsylvania Law and must register as such with the Pennsylvania Securities Commission. In *The Matter Of Global Conduit, Inc.*, 2000 Pa. Sec. LEXIS 161 (Pa. Sec. 2000). And the failure to have registered before earning your finder's fee is a violation of Section 301(a) of the 1972 Act, 70 P.S. § 1-301(a); *Global Conduit, Inc.*, 2000 Pa. Sec. LEXIS 161 (Pa. Sec. 2000).

The result is the same under federal law. You must be a broker dealer to earn a commission from a transaction involving the sale of securities, otherwise you are in violation of the law.

There are presently very few exceptions that allow a finders fee. Indeed, the most famous case is that of Paul Anka who had an agreement to receive a finder's fee for assisting in the raising of funds for a hockey team. Paul Anka, SEC No-Action Letter, [1991 Transfer Binder] Fed. Sec. L. Rep. (CCH), P 79, 797, at 78, 577 (July 24, 1991). 60 Bus. Law. 959. The SEC crafted a very narrow ruling to allow Anka to escape any penalties. In the Anka

case, the SEC stated that Anka would not be penalized because Mr. Anka:

1. had a bona fide, pre-existing business or personal relationship with these prospective investors;
2. reasonably believed those investors to be accredited;
3. would not advertise, endorse or solicit investors.
4. would have no personal contact with prospective investors;
5. would not provide financing for any investors;
6. would not advise on valuation;
7. would not perform due diligence on the Senators' offering;
8. had never been a broker-dealer or registered representative of a broker-dealer.

Essentially, Mr. Anka turned over a list of prospects to persons who were broker-dealers and they contacted the individuals. Mr. Anka did nothing else.

Most “finders” would have to do much more than this to get the deal to close.

Recognizing this problem, there are several proposals to change the law to allow a limited class of finders to earn finders fees without having to register as broker-dealers. See Report and Recommendations of the Task Force on Private Placement Broker-Dealers, ABA, The Business Lawyer, 60 Bus. Law. 959 (May, 2005).

If we can be of assistance to you in structuring an appropriate transaction, please feel free to contact Neal A. Jacobs at the Firm.

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