

# **PRIVATE PLACEMENTS, FINDERS' FEES AND STATE SECURITIES UPDATES**

**Denise Voigt Crawford  
Texas Securities Commissioner**

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# PRIVATE PLACEMENTS, FINDERS' FEES, AND STATE SECURITIES UPDATES

## I. Introduction.

The Texas Securities Act (“Act”) and the Rules and Regulations of the State Securities Board (“Rules”) are available on the Texas State Securities Board (“Board”) web site ([www.ssb.state.tx.us](http://www.ssb.state.tx.us)) or for purchase from the Agency at:

Texas State Securities Board  
P.O. Box 13167  
Austin, Texas 78711-3167  
512/305-8300 (voice)  
512/305-8310 (facsimile)  
[www.ssb.state.tx.us](http://www.ssb.state.tx.us)

## II. Changes to the Texas Securities Act.

The Act was last amended in the 78th Session of the Texas Legislature. An important clarification was made in the definition of “security;” authority was added for providing assistance to other state or foreign securities regulators; a penal provision was added for unregistered investment adviser activity; restitution authority was broadened to allow for equitable relief and disgorgement; and the fee provisions were restructured.

### A. Changes effective May 20, 2003.

Senate Bill 1060 contained four major substantive revisions to the Act. It passed both the House and Senate with no opposition and it became effective upon being signed by Governor Rick Perry.

1. **Section 4.A.** In Section 4, Definitions, the definition of “security” or “securities” was amended to address a problem created by the Court of Criminal Appeal’s decision in *Thomas v. State*, 65 S.W.3d 38 (Tx. Crim. App. 2001) whereby it determined, as a matter of first impression, that a written instrument is required for an “evidence of indebtedness” under the Act which defines “security” to include other evidence of indebtedness. In *Thomas*, the defendant’s conviction for fraudulently selling unregistered securities in the form of an “evidence of indebtedness” was overturned because, although he had induced a fellow church member to invest in his corporation, no writing evidenced the debt. Thomas improperly used the funds and then filed for bankruptcy, but neither he nor his corporation had issued any shares, notes, bonds or profit sharing arrangements to document the investment transactions.

In S.B. 1060, the definition of “security” was amended to provide that, “*The term applies regardless of whether the “security” or “securities” are evidenced by a written instrument.*”

2. **Section 28.C.** In order to facilitate greater cooperation and assistance between securities regulators of different jurisdictions, Section 28, Investigations, Investigatory Materials, and Registration Related Materials, was amended by the addition of subsection C. It allows the Securities Commissioner to provide assistance, for example, issue a subpoena in Texas, at the request of another state or foreign regulator. Such assistance may be provided to assist in conducting an investigation to determine whether a person has violated, is violating, or is about to violate a law or rule of another state or foreign jurisdiction relating to a matter the securities regulator is authorized to administer or enforce.

There are four conditions to be considered by the Commissioner in determining whether assistance is necessary or appropriate:

- whether the securities regulator is permitted and has agreed to provide assistance within the regulator’s jurisdiction to the Commissioner reciprocally and at the Commissioner’s request [concerning securities matters];
- whether compliance with the request for assistance would violate or otherwise prejudice the public policy of this state;
- whether the conduct described in the request would also constitute a violation of this Act or another law of this state had the conduct occurred in this state; and
- the availability of Board employees and resources of the Board or Commissioner necessary to carry out the request for assistance.

3. **Section 29.I.** A new subsection was added to Section 29, Penal Provisions, to provide a felony offense for a person who renders services as an investment adviser or investment adviser representative without being registered. This addition is directly parallel to the penal provision for acting as a dealer or agent without being registered. It provides that a person who renders services as an investment adviser or an investment adviser representative without being registered as required by the Act shall be deemed guilty of a felony and on conviction shall be sentenced to pay a fine of not more than \$5,000 or imprisonment in the penitentiary for not less than two or more than ten years, or by both the fine and imprisonment.

4. **Section 32.B and C.** Section 32, Injunctions and Restitution, was amended to add language to subsection B that broadens the relief a victim of fraudulent practices can receive. **“Equitable relief”** was added to the category of relief (which includes restitution) that can be sought by the Attorney General at the request of the Securities Commissioner. In addition, language was added authorizing a district court to “grant any equitable relief that the court considers appropriate” and to order a defendant to deliver to the person defrauded the amount of money or property that the defendant obtained from the person by fraudulent practices.

A new subsection C was added authorizing the Attorney General, at the request of the Securities Commissioner, to seek the **disgorgement of any economic benefit** gained by a defendant through a fraud or fraudulent practice, including *a bonus, fee, commission, option, proceeds, profit from or loss avoided through the sale of the security, or any other tangible relief.*

**B. Change effective June 20, 2003.**

**Section 35.** House Bill 1840 amended Section 35, Fees, to authorize the State Securities Board to establish and set certain fees in amounts that are reasonable and necessary. The fees were to be set at a level sufficient to cover the cost of administering and enforcing the Act in excess of the amount generated by the fees as they existed on September 1, 2002. Although this amendment provides flexibility for the Board to set fees necessary to administer and enforce the Act, and it covers fees affecting securities registration, dealer and agent registration and renewal, and investment adviser and investment adviser representative registration and renewal, the actual amount appropriated is still decided by the legislature. It also covers notice filing fees for investment advisers and investment adviser representatives.

Since the amendment became effective, the Board has raised fees only once for two categories of fees: (1) for renewal of a dealer, agent, investment adviser or investment adviser representative, or for renewal of an investment adviser or investment adviser representative notice filing; and (2) for an original, amended, or renewal application to sell or dispose of securities or to notice file for selling federal covered securities. The fee in each category was increased by \$30.

**III. Significant Changes to the Board Rules made in 2004, 2005, and 2006.**

**A. Finder rules (§§115.1(a)(9), 115.3(c)(2)(E), and 115.11).**

Effective September 1, 2006, the Board adopted a series of rules intended to encourage capital formation by creating a limited registration for a person acting as a finder. This new rule gives small businesses an additional legal option in raising capital and assures that finders complying with the rule can legally collect fees for their activities.

A finder is defined as:

“an individual who receives compensation for introducing an accredited investor to an issuer or an issuer to an accredited investor solely for the purpose of a potential investment in the securities of the issuer, but does not participate in negotiating any of the terms of an investment and does not give advice to any such parties regarding the advantages or disadvantages of entering into an investment, and conducts this activity in accordance with §115.11 of this title (relating to Activities of a Finder). Note that an individual registered as a finder is not permitted to register in any other capacity; however, a registered general dealer is allowed to engage in finder activity without separate registration as a finder.”

The most significant aspect of the new rule is that a finder can receive **compensation solely for introducing** accredited investors to a company issuing securities and/or introducing an issuer to accredited investors.

An individual who applies for registration as a finder receives a full waiver from the Agency’s usual examination requirements. Finder registration requires the filing of a Form BD (Uniform Application for Broker Dealer Registration), available on the Agency’s website, and payment of a \$275 registration fee. Registration is valid for a calendar year and may be renewed annually.

A finder is prohibited from participating in negotiating any of the terms of an investment and is not permitted to give advice to the parties regarding the advantages or disadvantages of entering into an investment.

This is an example of finder activity:

Mr. A knows Mr. B, an accredited investor, from a preexisting social or business relationship. Mr. A knows that Mr. B is looking for an investment opportunity. Mr. A also knows Mr. C, who has a company in need of investors.

After registering as a finder, Mr. A can received a fee from Mr. B and/or from Mr. C’s company for introducing Mr. B to Mr. C. Mr. A can do nothing more than make the introduction, either in person or by providing contact information so that Mr. B and Mr. C can contact each other.

Mr. A cannot advise Mr. B on whether Mr. C’s company is a good investment. He can not accept Mr. B’s investment funds or even deliver them to Mr. C. Simply put, Mr. A can only make the introduction, then walk away and let the two parties take it from there.

**B. Hedge Fund Adviser rule (§109.6).**

An investment adviser to a private fund has always been subject to registration in Texas if the fund has natural persons as investors. An exemption borne out of Section 5.H of the Act has provided an exemption for an adviser to institutional investors, such as private funds with investors consisting of non-natural person participants. In 1997, a no-action request letter was submitted asking whether an adviser to a hedge fund with natural person investors was subject to registration requirements. The response from the staff was in the affirmative. Subsequently, members of the Texas Bar asked staff of the Agency to develop a proposal for amending §109.3 to clarify its applicability to hedge funds. The result is §109.6, Investment Adviser Registration Exemption for Investment Advice to Financial Institutions and Certain Institutional Investors, adopted by the Board in 2005.

Subsection (c), regarding investment advice rendered to natural persons and private funds, provides that there is no exemption for an investment adviser providing investment advisory services to a natural person or to a private fund, such as a hedge fund, that is composed partially or entirely of natural persons. The rule defines “private fund” as an entity that:

- (1) would be subject to regulation under the federal Investment Company Act of 1940 but for the exceptions from the definition of “investment company” provided for:
  - (A) a fund that has no more than 100 beneficial owners, or
  - (B) a fund that is owned exclusively by qualified purchasers who acquired ownership through a non-public offering;
- (2) permits investors who are natural persons to redeem their interests in the fund within two years of purchasing them; and
- (3) offers interests in the entity based on the investment advisory skills, ability or expertise of the investment adviser.

Due to the current uncertainties at the federal level regarding the appropriate level of regulation over hedge fund activities, it is possible that this rule may be revisited in the future.

**C. Individual Accredited Investor Exemption (§139.16).**

In 2005, the Board acted to stem an abuse of the Individual Accredited Investor Exemption by explicitly addressing investment intent of purchasers. Certain opinion letters were being circulated that opined that Rule 139.16 could be used as a state

exemption in coordination with Regulation D, Rule 504 offerings, resulting in shares that were free trading.

The staff agrees that §139.16 can be used in coordination with Rule 504 offerings, but not that the shares are freely tradable. The writers of these opinion letters were taking advantage of the fact that §139.16 did not expressly set forth an investment intent requirement for purchasers. In reviewing the rule making history of §139.16, it is abundantly clear that the Board's intent at the time of adoption (1995) was to provide an issuer exemption that would result in restricted securities. Therefore, the Board acted in 2005 to thwart the abuse by amending the rule to include an express investment intent similar to the language in the §109.13 Limited Offering Exemption. New subsection (k) of the rule, regarding investment intent, provides that:

The issuer and any person acting on its behalf shall exercise reasonable care to assure that the purchasers are acquiring the securities as an investment. Such reasonable care should include, but not be limited to, the following:

- (1) having reasonable grounds to believe and, after making reasonable inquiry, believe that the purchaser is acquiring the securities with investment intent for his or her own account or on behalf of other persons and not for resale or with a view toward distribution;
- (2) placing a legend on the certificate or other document evidencing the securities to the effect that the securities have not been registered under any securities law and setting forth or referring to the restrictions on transferability and sale of the securities;
- (3) issuing stop transfer instructions to the issuer's transfer agent, if any, with respect to the securities, or, if the issuer transfers its own securities, making a notation in the appropriate records of the issuer; and
- (4) obtaining from the purchaser a signed written agreement to the effect that the securities will not be sold without registration under applicable securities laws or exemptions therefrom.

**D. Exemption for Investment Adviser to High Net Worth Family Entity (§139.22).**

In 2004, the Board adopted new rule §139.22, concerning an exemption from investment adviser registration for persons rendering investment advice to a high net worth family entity. The rule provides an exemption from registration for an

investment adviser to a “family entity” with a minimum aggregate net worth of \$5 million and is conditioned upon the firm or individual not holding itself out to the public as an investment adviser.

For purposes of this rule, a “high net worth family entity” is a corporation, limited partnership, limited liability company, or other entity, with all of its owners, partners, or members belonging to a single family who are all related by blood, adoption or marriage. In addition, the family entity must have a combined net worth of not less than \$5 million and the ownership by individual family member must be direct or indirect pursuant to a trust or other similar arrangement where the investment is made by or on behalf, or for the benefit, of the individual. Finally, an individual shall not constitute a “family entity” for purposes of this exemption regardless of the net worth of the individual.

In determining “net worth” for purposes of this rule, an investment adviser may rely on the entity’s most recent annual balance sheet or other financial statement which shall have been audited by an independent accountant or which shall have been verified under oath by a principal of the entity.

#### **IV. Other Significant Changes to the Board Rules relating to Dealers and Investment Advisers.**

##### **A. Amendment to §115.1, Definitions.**

“Branch office” is defined as “any location where one or more agents of a dealer regularly conduct the business of effecting any transactions in, or inducing or attempting to induce the purchase or sale of, any security, or that is held out as such.” The amendment was made in 2006 to coordinate with the adoption of Form BR, the Uniform Branch Office Form, which is used by all states that register branch offices and by the NASD. The definition and form were developed jointly by the North American Securities Administrators Association (NASAA), and the NASD.

The branch office definition excludes:

- (1) any location that is established solely for customer service and/or back office type functions where no sales activities are conducted and that is not held out to the public as a branch office;
- (2) any location that is the agent’s primary residence, provided that:
  - (a) only one agent, or multiple agents who reside at that location and are members of the same immediate family, conduct business at the location;

- (b) the location is not held out to the public as an office and the agent does not meet with customers at the location;
  - (c) neither customer funds nor securities are handled at that location;
  - (d) the agent is assigned to a designated branch office, and such designated branch office is reflected on all business cards, stationery, advertisements, and other communications to the public by such agent;
  - (e) the agent's correspondence and communications with the public are subject to the dealer's supervision;
  - (f) electronic communications (e.g., e-mail) are made through the dealer's electronic system;
  - (g) all orders are entered through the designated branch office or an electronic system established by the dealer that is reviewable at the branch office;
  - (h) written supervisory procedures pertaining to supervision of sales activities conducted at the residence are maintained by the dealer; **and**
  - (i) a list of the residence locations are maintained by the dealer;
- (3) any location, other than a primary residence, that is used for securities business for less than 30 business days in any one calendar year, provided the dealer complies with the provisions of clause (ii)(II) - (VIII) of this subparagraph;
  - (4) any office of convenience, where agents occasionally and exclusively by appointment meet with customers, which is not held out to the public as an office;
  - (5) any location that is used primarily to engage in non-securities activities and from which the agent(s) effects no more than 25 securities transactions in any one calendar year; provided that any advertisement or sales literature identifying such location also sets forth the address and telephone number of the location from which the agent(s) conducting business at the non-branch locations are directly supervised;

- (6) the floor of a registered national securities exchange where a dealer conducts a direct access business with public customers; and
- (7) a temporary location established in response to the implementation of a business continuity plan.

**B. Amendment to §115.5, Minimum Records.**

Several new recordkeeping requirements were added in 2003 that focus on better documentation by dealers regarding customer account information and investment objectives. For example, for each new account with a natural person as a customer or owner, the dealer is required to keep an account record including the customer's name, tax identification number, address, telephone number, date of birth, employment status, annual income, net worth, and the customer's account investment objectives. A dealer is to furnish to each customer a copy of the account record containing such information and prominently state that the customer should mark any corrections and return the account record to the dealer. The dealer must also let the customer know that the customer should notify the dealer of any future changes to information contained in the account record. When there is a change in the account's investment objectives the dealer must furnish to the customer a copy of the updated customer account record on or before the thirtieth day after the date the dealer received notice of the change or changes.

Upon inspection by examiners from the Board, these and other recordkeeping requirements added to §115.5 can assist a dealer in demonstrating that their agents know their customers' account information and investment objectives. These records also facilitate expedited review of records by Agency staff during onsite examinations.

Recordkeeping requirements were also added detailing information a dealer must maintain regarding employees and agents, such as a listing of every agent of the dealer that shows, for each agent, every office of the dealer where the agent regularly conducts the business of handling funds or securities or effecting any transaction in, or inducing or attempting to induce the purchase or sale of any security for the dealer, and the Central Registration Depository number and every internal identification number or code assigned to that agent by the dealer.

Additions were made to require a dealer to make and keep records current, to maintain and preserve them in an easily accessible place, and to maintain records for various periods of time relative to the nature of a particular record that coordinate with maintenance and preservation requirements at the federal level.

The changes improve the ability of registered dealers to carry out their supervisory duties, help the Board's examiners conduct more efficient inspections, and coordinate better with recordkeeping rules applicable to federally registered dealers.

**C. Amendment to §116.10, Supervisory Requirements.**

The supervisory systems requirement for investment advisers was amended in 2006 to clarify that such systems are required to be in writing. The requirements are very general so that a registered person has the flexibility to design and implement a system of a size and nature that is reasonable in relation to the investment adviser's business operations. The SEC had already required investment advisers to have written supervisory requirements and the states have begun to add the express "written" requirement so that small investment advisers - even sole practitioners - will establish and maintain written supervisory procedures.

Supervisory systems must be written and available for immediate inspection by the Board's examiners in either print or electronic format. This requirement serves two distinct purposes: (1) it provides an examiner with a readily available set of supervisory requirements created and maintained by an investment adviser that the examiner can use to determine the adviser's and investment adviser representatives' compliance with supervisory procedures of the adviser, and (2) it provides a management tool for an investment adviser's use when an investment adviser representative fails to comply with the firm's supervisory system.

Strong supervisory systems place more focus on prevention and detection of violations and make high-level personnel more responsible for implementing and overseeing an investment adviser's compliance program. Importantly, the amendment requiring written supervisory systems also puts more emphasis on not just having a compliance program, but having an effective compliance program. By having written supervisory procedures, firms have a process to track the development, maintenance and updating of their supervisory systems. The Board's examiners are very focused on whether firms of all sizes are adequately supervising their employees, investment adviser representatives, and restricted representatives such as solicitors, particularly those in branch offices.

**V. Changes to the Board Rules relating to Exempt Transactions and Exempt Securities.**

**A. Transactions Exempt from Registration.**

Section 5 of the Act, Exempt Transactions, provides exemptions for a number of securities transactions. Subsection H provides an exemption for the sale of any security to certain listed institutions, such as a bank or trust company. Over the years, the Board adopted rules in Chapter 109 that expand the list of institutions listed in the Act to include sales to other categories of financial institutions and certain institutional investors.

In 2005, the Board adopted new §109.4, concerning the securities registration exemption for sales to financial institutions and certain institutional investors; §109.5, concerning the dealer registration exemption for sales to financial institutions and certain institutional investors; and §109.6, concerning the investment adviser

registration exemption for investment advice to financial institutions and certain institutional investors. (For additional discussion of §109.6, see III.B., above.)

Sections 109.4 - 109.6 are based on exemptions formerly found in §109.3. Amended §109.3 retains the definition of “savings institution” previously located in subsection (a) of the prior version of the rule. New § 109.4 sets forth the securities registration exemption previously located in §109.3, and new §109.5 contains the dealer exemption that was previously described in §109.3.

The most significant revision in this series is §109.6. The exemption from investment adviser registration, setting forth the Board’s long-standing position that an investment adviser to an entity composed partially or entirely of natural persons is not exempt from registration. Natural persons simply are not institutional investors, regardless of their net worth or annual income. Likewise, a private investment entity, such as a hedge fund, composed partially or entirely of natural persons, does not equate to an institutional investor. Section 109.6 provides an exemption from registration for an investment adviser to a traditional venture capital fund because a fund of this type does not have natural person investors and, therefore, does not constitute a “private fund” as that term is defined in §109.6(c).

Section 109.6 includes clarification as to when an investment adviser or investment adviser representative is providing investment advisory services to an entity and not to the owners of the legal entity, and provides a definition of a “private fund” so that investors who are not natural persons may be permitted to redeem their interests in the fund within two years of purchase without triggering a registration requirement for an adviser to a private fund as that term is defined.

## **B. Securities Exempt from Registration.**

Section 6 of the Act, Exempt Securities, provides exemption from registration for certain securities. Subsection F provides an exemption for securities which at the time of sale have been listed on an exchange named in subsection F. Among the list are securities “designated or approved for designation on notice of issuance on the national market system of the NASDAQ stock market ...”

In 2006, the Board adopted an amendment to §111.2 adding new subsection (f), to define the “national market system of the NASDAQ Stock Market,” as used in the Act, Section 6.F, to include only the NASDAQ Global Select Market, NASDAQ Global Market, and NASDAQ Capital Market.

# APPENDIX A

## THE TEXAS SECURITIES ACT

### (Excerpts)

As Amended, Including Significant Changes Effective as of September 1, 2003

*Italic faced type indicates amendments by the 78th Legislature  
(Note: No changes to the Act were made by the 79th Legislature)*

#### Sec. 4. Definitions.

The following terms shall, unless the context otherwise indicates, have the following respective meanings:

A. The term “security” or “securities” shall include any limited partner interest in a limited partnership, share, stock, treasury stock, stock certificate under a voting trust agreement, collateral trust certificate, equipment trust certificate, preorganization certificate or receipt, subscription or reorganization certificate, note, bond, debenture, mortgage certificate or other evidence of indebtedness, any form of commercial paper, certificate in or under a profit sharing or participation agreement, certificate or any instrument representing any interest in or under an oil, gas or mining lease, fee or title, or any certificate or instrument representing or secured by an interest in any or all of the capital, property, assets, profits or earnings of any company, investment contract, or any other instrument commonly known as a security, whether similar to those herein referred to or not. *The term applies regardless of whether the “security” or “securities” are evidenced by a written instrument.* Provided, however, that this definition shall not apply to any insurance policy, endowment policy, annuity contract, optional annuity contract, or any contract or agreement in relation to and in consequence of any such policy or contract, issued by an insurance company subject to the supervision or control of the Texas Department of Insurance when the form of such policy or contract has been duly filed with the Department as now or hereafter required by law.

\* \* \*

#### Sec. 28. Investigations, Investigatory Materials, and Registration Related Materials.

\* \* \*

C. *Assistance to Securities Regulator of Another Jurisdiction.* *The Commissioner may provide assistance to a securities regulator of another state or a foreign jurisdiction who requests assistance in conducting an investigation to determine whether a person has violated, is violating, or is about to violate a law or rule of the other state or foreign jurisdiction relating to a securities matter the securities regulator is authorized to administer or enforce. The Commissioner may provide assistance by using the authority to investigate and any other power conferred by this*

*section as the Commissioner determines is necessary and appropriate. In determining whether to provide the assistance, the Commissioner may consider:*

*(1) whether the securities regulator is permitted and has agreed to provide assistance within the regulator's jurisdiction to the Commissioner reciprocally and at the Commissioner's request concerning securities matters;*

*(2) whether compliance with the request for assistance would violate or otherwise prejudice the public policy of this state;*

*(3) whether the conduct described in the request would also constitute a violation of this Act or another law of this state had the conduct occurred in this state; and*

*(4) the availability of Board employees and resources of the Board or Commissioner necessary to carry out the request for assistance.*

**Sec. 29. Penal Provisions.**

Any person who shall:

\* \* \*

*I. Render services as an investment adviser or an investment adviser representative without being registered as required by this Act shall be deemed guilty of a felony and on conviction of the felony shall be sentenced to pay a fine of not more than \$5,000 or imprisonment in the penitentiary for not less than two or more than 10 years, or by both the fine and imprisonment.*

**Sec. 32. Injunctions and Restitution.**

\* \* \*

*C. In an action brought under this section for fraud or a fraudulent practice in connection with the sale of a security, the Attorney General may seek, for an aggrieved person, the disgorgement of any economic benefit gained by the defendant through the violation, including a bonus, fee, commission, option, proceeds, profit from or loss avoided through the sale of the security, or any other tangible benefit. The Attorney General may recover from an order of disgorgement obtained under this subsection reasonable costs and expenses incurred by the Attorney General in bringing the action.*

**Sec. 35. Fees.**

*A. The Board shall establish the following fees in amounts so that the aggregate amount that exceeds the amount of the fees on September 1, 2002, produces sufficient revenue to cover the costs of administering and enforcing this Act:*

(1) *for the filing of any original, amended, or renewal application to sell or dispose of securities, an amount not to exceed \$100;*

(2) *for the filing of any original application of a dealer or investment adviser or for the submission of a notice filing for a federal covered investment adviser, an amount not to exceed \$100;*

(3) *for the filing of any renewal application of a dealer or investment adviser or for the submission of a renewal notice filing for a federal covered investment adviser, an amount not to exceed \$100;*

(4) *for the filing of any original application for each agent, officer, or investment adviser representative or for the submission of a notice filing for each representative of a federal covered investment adviser, an amount not to exceed \$100; and*

(5) *for the filing of any renewal application for each agent, officer, or investment adviser representative or for the submission of a renewal notice filing for each representative of a federal covered investment adviser, an amount not to exceed \$100.*

**B.** The Commissioner or Board shall charge and collect the following fees and shall daily pay all fees received into the State Treasury:

(1) *for any filing to amend the registration certificate of a dealer or investment adviser or evidence of registration of an agent or investment adviser representative, issue a duplicate certificate or evidence of registration, or register a branch office, \$25;*

(2) *for the examination of any original or amended application filed under Subsection A, B, or C of Section 7 of this Act, regardless of whether the application is denied, abandoned, withdrawn, or approved, a fee of one-tenth (1/10) of one percent (1%) of the aggregate amount of securities described and proposed to be sold to persons located within this state based upon the price at which such securities are to be offered to the public;*

(3) *for certified copies of any papers filed in the office of the Commissioner, the Commissioner shall charge such fees as are reasonably related to costs; however, in no event shall such fees be more than those which the Secretary of State is authorized to charge in similar cases;*

(4) *for the filing of any application for approval of a stock exchange so that securities fully listed thereon will be exempt, a fee of \$10,000;*

(5) *for the filing of a request to take the Texas Securities Law Examination, \$35;*

(6) *for the filing of an initial notice required by the Commissioner to claim a secondary trading exemption, a fee of \$500, and for the filing of a secondary trading exemption renewal notice, a fee of \$500;*

(7) *for the filing of an initial notice required by the Commissioner to claim a limited offering exemption, a fee of one-tenth (1/10) of one percent (1%) of the aggregate amount of securities described as being offered for sale, but in no case more than \$500; and*

(8) *for an interpretation by the Board's general counsel of this Act or a rule adopted under this Act, a fee of \$100, except that an officer or employee of a governmental entity and the entity that the officer or employee represents are exempt from the fee under this subsection when the officer or employee is conducting official business of the entity.*

*C. Subject to Subsection A of this section, the Board shall set a fee under this section in an amount that is reasonable and necessary to defray costs.*

*D. A cost incurred by the Board in administering this Act may be paid only from a fee collected under Subsection A of this section.*

### **Sec. 35-1. Fees for Sales of Excess Securities.**

A. An offeror who sells securities in this State in excess of the aggregate amount of securities registered for the offering may apply to register the excess securities by paying three times the difference between the initial fee paid and the fee required under Subsection *B(2)* of Section 35, plus, if the registration is no longer in effect, interest on that amount computed at the rate provided by Section 302.002, Finance Code, from the date the registration was no longer in effect until the date the subsequent application is filed, for the securities sold to persons within this State, plus the amendment fee prescribed by Subsection *A(1)* of Section 35. Registration of the excess securities, if granted, shall be effective retroactively to the effective date of the initial registration for the offering.

B. An offeror who has filed a notice to claim a limited offering exemption, who paid less than the maximum fee prescribed in Subsection *B(7)* of Section 35, and who offered a greater amount of securities in the offering than authorized pursuant to the formula prescribed in Subsection *B(7)* of Section 35, may file an amended notice disclosing the amount of securities offered and paying three times the difference between the fee initially paid and the fee which should have been paid, plus interest on that amount computed at the rate provided by Section 302.002, Finance Code, from the date the original notice was received by the Commissioner until the date the amended notice is received by the Commissioner. The amended notice shall be retroactive to the date of the initial filing.

### **Sec. 35-2. Fees for Sales of Unregistered Securities.**

If, after notice and hearing, the Commissioner or any court of competent jurisdiction finds that an offeror has sold securities in this State pursuant to an offering no part of which has been registered under Section 7 or 10 of this Act and for which the transactions or securities are not exempt under Section 5 or 6 of this Act, the Commissioner or said court may impose a fee equal to six times the amount that would have been paid if the issuer had filed an application to register the securities and paid the fee prescribed by Subsection *B(2)* of Section 35 based on the aggregate

amount of sales made in this State within the prior three years, plus interest on that amount at the rate provided by Section 302.002, Finance Code, from the date of the first such sale made in this State until the date the fee is paid. The payment of the fee prescribed by this Section does not effect registration of the securities or affect the application of any other Section of this Act. The payment of the fee prescribed by this Section is not an admission that the transactions or securities were not exempt and is not admissible as evidence in a suit or proceeding for failure to register the securities.

**APPENDIX B**

**SELECTED RULES OF THE  
TEXAS STATE SECURITIES BOARD**

**(Excerpts)**

*(Located in Title 7 of the Texas Administrative Code)*

**Rule 109.6. Investment Adviser Registration Exemption for Investment Advice to Financial Institutions and Certain Institutional Investors.**

- (a) **Availability.** The exemption from investment adviser and investment adviser representative registration provided by the Texas Securities Act, Section 5.H, or this section is not available if the financial institution or other institutional investor named therein is in fact acting only as agent for another purchaser that is not a financial institution or other institutional investor listed in Section 5.H or this section. These exemptions are available only if the financial institution or other institutional investor named therein is acting for its own account or as a bona fide trustee of a trust organized and existing other than for the purpose of acquiring the investment advisory services for which the investment adviser or investment adviser representative is claiming the exemption. For purposes of this section, an investment adviser or investment adviser representative that is providing investment advisory services to a corporation, general partnership, limited partnership, limited liability company, trust or other legal entity, other than a private fund, is not providing investment advisory services to a shareholder, general partner, member, other security holder, beneficiary or other beneficial owner of the legal entity unless the investment adviser provides investment advisory services to such owner separate and apart from the investment advisory services provided to the legal entity.
- (b) **Investment advice rendered to certain institutional investors.** The State Securities Board, pursuant to the Act, Section 5.T and Section 12.C, exempts from the investment adviser and investment adviser representative registration requirements of the Act, persons who render investment advisory services to any of the following:
- (1) an “accredited investor” (as that term is defined in Rule 501(a)(1)-(3), (7), and (8) promulgated by the Securities and Exchange Commission (SEC) under the Securities Act of 1933, as amended (1933 Act), as made effective in SEC Release Number 33-6389, as amended in Release Numbers 33-6437, 33-6663, 33-6758, and 33-6825);
  - (2) any “qualified institutional buyer” (as that term is defined in Rule 144A(a)(1) promulgated by the SEC under the 1933 Act, as made effective in SEC Release Number 33-6862, and amended in Release Number 33-6963); and

- (3) a corporation, partnership, trust, estate, or other entity (excluding individuals) having net worth of not less than \$5 million, or a wholly-owned subsidiary of such entity.
- (c) **Investment advice rendered to natural persons and private funds.** There is no exemption under this section for an investment adviser providing investment advisory services to a natural person or to a private fund, such as a hedge fund, that is composed partially or entirely of natural persons. A “private fund” is an entity that:
- (1) would be subject to regulation under the federal Investment Company Act of 1940 but for the exceptions from the definition of “investment company” provided for:
    - (A) a fund that has no more than 100 beneficial owners, or
    - (B) a fund that is owned exclusively by qualified purchasers who acquired ownership through a non-public offering;
  - (2) permits investors who are natural persons to redeem their interests in the fund within two years of purchasing them; and
  - (3) offers interests in the entity based on the investment advisory skills, ability or expertise of the investment adviser.
- (d) **Financial statements.** For purposes of determining an institutional investor’s total assets or net worth under this section, an investment adviser or investment adviser representative may rely upon the entity’s most recent annual balance sheet or other financial statement which shall have been audited by an independent accountant or which shall have been verified by a principal of the institutional investor.

*Source Note: The provisions of this §109.6 adopted to be effective July 14, 2005, 30 TexReg 3987.*

**Rule 115.1. General Provisions.**

- (a) **Definitions.** Words and terms used in this chapter are also defined in §107.2 of this title (relating to Definitions). The following words and terms, when used in this chapter, shall have the following meanings, unless the context clearly indicates otherwise.

\* \* \*

- (9) **Finder**--An individual who receives compensation for introducing an accredited investor to an issuer or an issuer to an accredited investor solely for the purpose of a potential investment in the securities of the issuer, but does not participate in negotiating any of the terms of an investment and does not give advice to any such parties regarding the advantages or disadvantages of entering into an investment, and conducts this activity in accordance with §115.11 of this title (relating to Activities of a Finder). Note that an individual registered as a finder is not permitted to register in any other capacity;

however, a registered general dealer is allowed to engage in finder activity without separate registration as a finder.

\* \* \*

**Rule 115.3. Examination.**

\* \* \*

**(c) Waivers of examination requirements.**

\* \* \*

- (2) A full waiver of the examination requirements of the Texas Securities Act, Section 13.D, is granted by the Board to the following classes of persons:

\* \* \*

- (E) a finder;

\* \* \*

*Source Note: The provisions of this §115.3 adopted to be effective August 12, 2001, 26 TexReg 5794; amended to be effective November 26, 2001, 26 TexReg 9581; amended to be effective July 14, 2005, 30 TexReg 3988; amended to be effective September 1, 2006, 31 TexReg 6712.*

**Rule 115.11. Activities of a Finder.**

**(a) Prohibited activities.** A finder shall not:

- (1) participate in negotiating any of the terms of an investment;
- (2) give advice to an accredited investor or an issuer regarding the advantages or disadvantages of entering into an investment;
- (3) conduct due diligence on behalf of a potential issuer or potential investor, provide valuation, or provide other analysis to an accredited investor or an issuer regarding an investment;
- (4) advertise to seek accredited investors or issuers;
- (5) have custody of an accredited investor's funds or securities;
- (6) serve as an escrow agent for the parties; or

- (7) disclose information to an accredited investor or to an issuer other than the information described in subsections (b) and (c) of this section.

**(b) Required disclosures.**

- (1) A finder must disclose the following to each accredited investor:
  - (A) that compensation will be paid to the finder;
  - (B) that the finder can neither recommend nor advise the accredited investor with respect to the offering; and
  - (C) any potential conflict of interest in connection with the finder's activities.
- (2) The disclosures required by paragraph (1) of this subsection must be provided in writing.

**(c) Permitted disclosures.**

- (1) A finder may provide to an accredited investor some or all of the following information:
  - (A) the name, address, and telephone number of the issuer of the securities;
  - (B) the name, a brief description, and price (if known) of any security to be issued;
  - (C) a brief description of the business of the issuer in 25 words or less;
  - (D) the type, number, and aggregate amount of securities being offered; and/or
  - (E) the name, address, and telephone number of the person to contact for additional information.
- (2) A finder may provide to an issuer contact information regarding an accredited investor.

**(d) Recordkeeping.**

- (1) A finder is not required to maintain the records listed in §115.5 of this title (relating to Minimum Records); however, compliance with the recordkeeping requirements of §115.5 of this title will satisfy the requirements of this subsection.
- (2) A finder shall maintain and preserve a copy of Form BD used to register the finder for a period of five (5) years from the date of the termination of the finder's registration.
- (3) A finder shall maintain and preserve for a period of five (5) years the following records related to transactions that are completed and to transactions where the finder receives compensation:

- (A) records of compensation received for acting as a finder, including the name of the payor, the date of payment, name of the issuer, and name of the accredited investor;
  - (B) copies of information provided by the finder to prospective accredited investors;
  - (C) any agreements and/or contracts between the finder and the accredited investor;
  - (D) any agreements and/or contracts between the finder and the issuer;
  - (E) any lists of contacts/prospective accredited investors and/or issuers; and
  - (F) any correspondence with accredited investors and/or issuers.
- (4) The records required to be maintained and preserved pursuant to this subsection must be maintained in a manner that will permit the immediate location of any particular document.
  - (5) The records required to be maintained and preserved pursuant to this subsection may be archived if they are more than two years old.
  - (6) A finder shall not commingle records to be maintained and preserved pursuant to this subsection with other records.
  - (7) A finder shall, upon written request of the Securities Commissioner, furnish to the Securities Commissioner any records required to be maintained and preserved under this subsection.
- (e) **Supervisory requirements.** Because a finder is an individual who will not have agents, a finder is not required to maintain a supervisory system as provided in §115.10 of this title (relating to Supervisory Requirements).

*Source Note: The provisions of this §115.11 adopted to be effective September 1, 2006, 31 TexReg 6713.*

**Rule 139.16. Sales to Individual Accredited Investors.**

- (a) **In general.** The State Securities Board, pursuant to the Securities Act, Section 5.T, exempts from the securities registration requirements of the Securities Act, Section 7, the offer and sale by the issuer or a registered dealer without advertising of any security to an individual accredited investor, or to any purchaser who the issuer has reasonable grounds to believe and after making reasonable inquiry shall believe to be an individual accredited investor, provided that such security is not part of the same distribution or offering as securities of the same issuer which have been registered or are proposed to be registered by pending application under the Securities Act, Section 7. “Advertising,” as used in this subsection, does not include the use

of limited use advertisements under subsection (e) of this section or the use of the type of printed material as permitted by §109.13(b) of this title (relating to Limited Offering Exemptions) in connection with an offering under the Act, Section 5.I.

**(b) Who may purchase; who constitutes the issuer for purposes of selling securities.**

- (1) Individual accredited investors. For purposes of this section, the term “individual accredited investor” shall mean any natural person whose individual net worth, or joint net worth with that person’s spouse, at the time of his or her purchase exceeds \$1 million or any natural person who had an individual income in excess of \$200,000 in each of the two most recent years or joint income with that person’s spouse in excess of \$300,000 in each of those years and has a reasonable expectation of reaching the same income level in the current year. The term “individual accredited investor” shall also include any self-directed employee benefit plan with investment decisions made solely by persons that are “individual accredited investors” as defined in this paragraph and the individual retirement account of any such individual accredited investor.
- (2) Issuer. For the purposes of subsection (a), the term “issuer” includes any director, officer, or employee of the issuer provided all the following conditions are satisfied:
  - (A) the director, officer, or employee was not hired for the purpose of offering or selling such securities;
  - (B) the director’s, officer’s, or employee’s activity involving the offer and sale of such securities is strictly incidental to his or her bona fide primary non-securities related work duties; and
  - (C) the director’s, officer’s, or employee’s compensation is based solely on the performance of other such duties, i.e., the director, officer, or employee does not receive any compensation for offering for sale, selling, or otherwise aiding in the sale of securities.

**(c) Disqualifications.**

- (1) No exemption under this section shall be available for the securities of any issuer if the issuer or registered dealer:
  - (A) within the last five years, has filed a registration statement which is the subject of a currently effective registration stop order entered by the United States Securities and Exchange Commission or any state securities administrator;
  - (B) within the last five years, has been convicted of any felony in connection with the offer, purchase, or sale of any security or any felony involving fraud or deceit;

- (C) is currently subject to any state or federal administrative enforcement order, entered within the last five years, finding fraud or deceit in connection with the purchase and sale of any security; or
  - (D) is currently subject to any order, judgment or decree of any court of competent jurisdiction, entered within the last five years, permanently restraining or enjoining such party from engaging in or continuing to engage in any conduct or practice involving fraud or deceit in connection with the purchase and sale of any security.
- (2) For purposes of this subsection and subsection (d) of this section only, the term “issuer” includes:
- (A) any of the issuer’s predecessors or any affiliated issuer;
  - (B) any of the issuer’s directors, officers, general partners, or beneficial owners of 10% or more of any class of its equity securities (beneficial ownership meaning the power to vote or direct the vote and/or the power to dispose or direct the disposition of such securities);
  - (C) any of the issuer’s promoters presently connected with the issuer in any capacity, including:
    - (i) any person who, acting alone or in conjunction with one or more other persons, directly or indirectly takes initiative in founding and organizing the business or enterprise of an issuer; or
    - (ii) any person who, in connection with the founding and organizing of the business or enterprise of an issuer, directly or indirectly receives in consideration of services or property, or both services and property, 10% or more of any class of securities of the issuer or 10% or more of the proceeds from the sale of any class of such securities; however, a person who receives such securities or proceeds either solely as underwriting commissions or solely in consideration of property shall not be deemed a promoter within the meaning of this clause if such person does not otherwise take part in founding and organizing the enterprise; or
  - (D) any underwriter of the issuer.
- (3) For purposes of this subsection and subsection (d) of this section only, the term “registered dealer” includes any of the registered dealer’s partners, directors, executive directors, or beneficial owners of 10% or more of any class of its equity securities (beneficial ownership meaning the power to vote or direct the vote and/or the power to dispose or direct the disposition of such securities).

**(d) Exceptions from disqualifications.** The prohibitions of subsection (c) of this section shall not apply if:

- (1) the party subject to the disqualification is duly licensed or registered to conduct securities related business in the state in which the order, judgment, or decree creating the disqualification was entered against such party; or
- (2) before the first offer under this section, the Securities Commissioner, or the court or regulatory authority that entered the order, judgment, or decree, waives the disqualification upon a showing of good cause.

**(e) Limited use advertisements.** Any limited use advertisement used in connection with an offering under this section must be filed with the Securities Commissioner ten days prior to use in this state. A limited use advertisement may be disseminated by any means, direct or indirect. A limited use advertisement shall contain only the statements required or permitted to be included therein by this subsection.

(1) A limited use advertisement shall contain the following items of information:

- (A) a brief description of the securities to be offered (e.g., description of class, size of offering, price, percentage of commission);
- (B) the name, address, and telephone number of the person to contact for additional information concerning the offering;
- (C) the address where offering material may be obtained; and
- (D) the following statement: “The securities have not been registered with or approved by the Texas Securities Commissioner and are being offered and sold pursuant to the exemption provided by §139.16 of the Rules and Regulations of the State Securities Board. This advertisement was filed with the Texas Securities Commissioner on or about (fill in date). The securities are being offered to, and may be purchased by, only those natural persons whose individual net worth, or joint net worth with that person’s spouse, at the time of purchase of the securities, exceeds \$1 million or natural persons who have an individual income in excess of \$200,000 in each of the two most recent years, or joint income with that person’s spouse in excess of \$300,000 in each of those years, and who have a reasonable expectation of reaching that same income level in the current year.”

(2) A limited use advertisement may include any one or more of the following items of information:

- (A) the name and address of the issuer of the securities;
- (B) a brief description of the business of the issuer; and

- (C) the name and address of the registered dealer(s) acting on the issuer's behalf in connection with the offering.
- (f) Any issuer relying on this exemption shall, upon written request, furnish to the Securities Commissioner the information furnished by the issuer or registered dealer to offerees. Any issuer relying on this exemption must maintain, for a period of at least three years, evidence of the basis for its belief that all purchasers were accredited investors at the time of purchase.
- (g) Transactions exempt under this section may be combined with offers and sales exempt under the Securities Act, Section 5.H, and §109.4 of this title (relating to Securities Registration Exemption for Sales to Financial Institutions and Certain Institutional Investors). In this event, the statement required by subsection (e)(1)(D) of this section may be modified to indicate that the securities are also being offered to eligible purchasers under Section 5.H and §109.4 of this title (relating to Securities Registration Exemption for Sales to Financial Institutions and Certain Institutional Investors).
- (h) Because this exemption permits limited use advertisements, use of this exemption under certain circumstances could result in other exemptions not being available for other sales due to prohibitions in such exemptions against public solicitation and advertisements. Therefore, issuers or registered dealers who use this exemption should take all necessary steps to document that any sales to persons who are not individual accredited investors, as defined, were not made in response to a limited use advertisement. Users of this section should consult with experienced securities counsel, especially if they anticipate selling, within six months of the last sale made under this section, to any persons who are not individual accredited investors.
- (i) The use of a limited use advertisement in compliance with this section and in connection with sales under this section will not render exemptions that prohibit public solicitation or advertisements unavailable to sales that are made more than six months after the use of the limited use advertisement.
- (j) Should the offer and sale of securities fail, for any reason, to comply with all the terms and conditions for use of this section, the issuer may claim the availability of any other applicable exemption. A limited use advertisement that results in an offer to a person who is not an individual accredited investor within the meaning of this section does not alone result in loss of the exemption.
- (k) Investment intent; resales. The issuer and any person acting on its behalf shall exercise reasonable care to assure that the purchasers are acquiring the securities as an investment. Such reasonable care should include, but not be limited to, the following:
  - (1) having reasonable grounds to believe and, after making reasonable inquiry, believe that the purchaser is acquiring the securities with investment intent for his or her own account or on behalf of other persons and not for resale or with a view toward distribution;

- (2) placing a legend on the certificate or other document evidencing the securities to the effect that the securities have not been registered under any securities law and setting forth or referring to the restrictions on transferability and sale of the securities;
- (3) issuing stop transfer instructions to the issuer's transfer agent, if any, with respect to the securities, or, if the issuer transfers its own securities, making a notation in the appropriate records of the issuer; and
- (4) obtaining from the purchaser a signed written agreement to the effect that the securities will not be sold without registration under applicable securities laws or exemptions therefrom.

*Source Note: The provisions of this §139.16 adopted to be effective April 21, 1995, 20 TexReg 2622; amended to be effective December 27, 1995, 20 TexReg 10593; amended to be effective July 14, 2005, 30 TexReg 3990; amended to be effective January 8, 2006, 30 TexReg 8869.*

**Rule 139.22. Exemption for Investment Adviser to a High Net Worth Family Entity.**

- (a) The State Securities Board, pursuant to the Texas Securities Act, Section 5.T and Section 12.C, exempts an investment adviser and its investment adviser representatives from the registration requirements of the Act, Section 12, when such adviser:
  - (1) renders services as an investment adviser to a high net worth family entity or related family entities, and
  - (2) does not hold itself out to the public as one who renders services as an investment adviser.
- (b) For purposes of this section, a "high net worth family entity" is a corporation, limited partnership, limited liability company, or other entity, with all of its owners, partners, or members belonging to a single family who are all related by blood, adoption or marriage; with a combined net worth of not less than \$5 million; and with ownership by an individual family member being direct or indirect pursuant to a trust or other similar arrangement where the investment is made by or on behalf of, or for the benefit of, the individual. An individual shall not constitute a "family entity" for purposes of this exemption regardless of the net worth of the individual.
- (c) For purposes of determining "net worth" under this section, an investment adviser may rely on the entity's most recent annual balance sheet or other financial statement which shall have been audited by an independent accountant or which shall have been verified under oath by a principal of the entity.

*Source Note: The provisions of this §139.22 adopted to be effective October 25, 2004, 29 TexReg 9825.*