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Topic: RSS Feed
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A "TIC"ING TIME BOMB: RULE 506 MEETS SECTION 1031

Fordham Journal of Corporate & Financial Law, 2007 by Whitman, Elizabeth Ayres

- « Previous
- 1
- ...
- 11
- 12
- 13
- 14
- 15
- 16
- 17
- 18
- 19
- ...
- 23
- Next »

Payment of finder's fees by securities broker-dealers, if permitted, could provide some compensation for these referring parties while giving the securities broker-dealers access to a larger pool of prospective TIC investors at that critical early point before sale of their relinquished property. SEC no-action letters provide little guidance on the permissibility of finder's fees in TIC transactions. In Colonial Equities Corp.,133 the SEC Division of Market Regulation issued a no-action letter where an issuer of real estate limited partnerships sold as private placements proposed to pay a flat fee to insurance agencies for referring potential investors.134 In Paul Anka,135 the SEC issued a no-action letter where Mr. Anka proposed to provide the Ottawa Senators, a hockey team, with names and contact information for persons with whom he had a relationship so that the Senators could contact those persons about the purchase of limited partnership interests. Mr. Anka would not contact any prospective investors or otherwise promote the limited partnership interests but would receive, as compensation, ten percent of the sales price of any interests purchased by persons he recommended.136 Earlier, in Mona/Kauai Corporation,137 the SEC issued a no-action letter where an issuer proposed payment of a compensation to real estate brokers whose activity was limited to providing names of prospective purchasers for the condominiums, with the referral fee being two to three percent of the sale price, payable only if the issuer actually sold a condominium to the prospective purchaser.138

More recently, however, in John R. Wirthlin,139 the SEC declined to issue a no-action letter where Mr. Wirthlin proposed to make introductions between accountants and other professionals who had clients seeking section 1031 replacement property and registered representatives selling real estate limited partnership interests.140 Mr. Wirthlin was to be paid a percentage of the sales price by the issuer of the limited partnership interests if a sale was consummated.141 The SEC distinguished finders for issuers from finders for broker-dealers and also expressed concern about Mr. Wirthlin's intention to solicit accountants and other professionals, attend the meeting between those professionals and the broker-dealer, and receive transaction-based compensation.142 In 2000, the SEC revoked its prior no-action letter in Dominion Resources, Inc.143 For many years, Dominion Resources had, under SEC sanction through a no-action letter, been assisting issuers with structuring securities transactions in exchange for a negotiated fee payable only if the transactions were consummated.144

Moreover, the NASD has indicated disapproval of finder's fee arrangements. NASD Conduct Rule 2460 provides that the NASD

consistently has taken the position . . . that it is improper for a member or a person associated with a member to make payments of 'finders' or referral fees to third parties who introduce or refer prospective brokerage customers to the firm, unless the recipient is registered as a representative of an NASD member firm.

- « Previous
- 1
- ...
- 11
- 12
- 13
- 14
- 15
- 16
- 17
- 18
- 19
- ...
- 23
- Next »