

UNLOCKING LIQUIDITY IN PRIVATE MARKETS

Understanding Tender Offers for Employees and Early Investors via Secondary Marketplaces

Overview

The path to liquidity for private company stakeholders has historically been through an IPO or acquisition. However, as private companies, particularly those that have attained "unicorn" status, remain private longer and valuations grow, employees and early investors often face challenges converting their equity into cash.

An increasingly common solution to achieve at least partial liquidity is through tender offers facilitated by secondary marketplaces - examples include Nasdaq Private Market (NPM), Forge Global, and Carta. These platforms provide vital infrastructure for conducting compliant, transparent, and efficient secondary transactions, enabling stakeholders to realize value before a public exit.

Tender Offers

A tender offer is a liquidity event designed to enable stockholders in a private company to sell some or all of their shares to another investor or back to the company. In practice, this offers both employees and early investors the opportunity to convert at least part of their equity into cash without having to wait indefinitely for the company to be sold or go public.

The relevant company retains control of the process throughout by deciding who can participate (who sells and who buys), how much stock can be sold (partial or full liquidity), the share price, and whatever information is to be disclosed in association with the transaction.

Benefits of Tender Offers

To the issuing company:

- Increased employee satisfaction and retention
- Controlled and compliant secondary activity
- Data and insights into shareholder sentiment and market valuation
- Enhanced reputation for future talent and capital raising

The Growth of Private Market Unicorns

What is a unicorn?

A venture capital-backed company valued at **\$1+ billion**

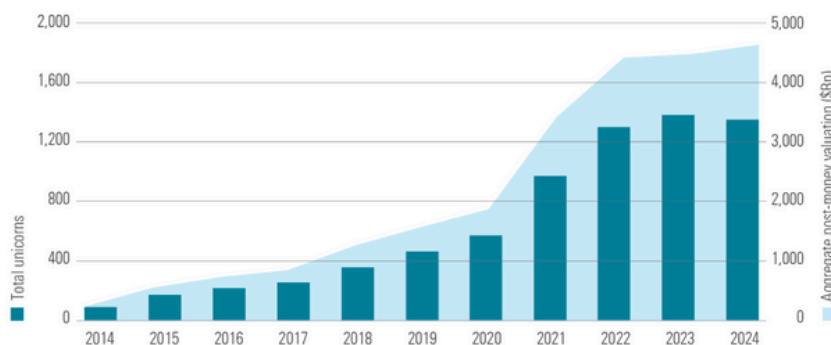
Number of unicorns globally

1,300+

Approximate value

\$4.5 trillion

The growth of unicorns



Source: "Unicorns and the Growth of Private Markets." Morningstar Indexes, 30 Apr. 2024

To the selling individual shareholder:

- De-risk and take some “chips off the table” in a highly appreciated investment scenario
- Better incorporate proceeds from an outsized concentration into a holistic financial plan and investment strategy
- Better manage tax implications – particularly if there are offsetting losses elsewhere
- Fund other goals consistent with financial plan, philanthropic intent, or wealth transfer strategies

Structure of a Tender Offer

Tender offers typically include:

- Issuer-led or shareholder-led structures
- Fixed-price or Dutch auction pricing
- Defined offer windows (e.g., 2-4 weeks)
- Legal and tax compliance (Rule 701, 409A, Blue Sky laws)
- Use of a transfer agent and brokerage services for settlement

Selling Shareholders: How It Works

For selling shareholders (employees and early investors), the tender offer process can often unfold as follows:

- **Notification:** The company notifies eligible shareholders of an upcoming tender offer, outlining price, quantity limits, and eligibility criteria.
- **Participation Decision:** Shareholders review offer documents and decide whether to sell some or all of their eligible shares. They may need to consult with their legal, tax, and financial advisors.
- **Submission:** Participants submit intent to sell via the platform (e.g., NPM, Forge, or Carta). Platforms typically have a secure portal for uploading documents and confirming share eligibility.
- **Approval and Clearance:** The company or transfer agent verifies eligibility and ensures compliance with internal governance documents (e.g., ROFR, investor rights agreements).
- **Execution:** Once the offer closes, shares are transferred from the selling shareholders to the approved buyers (usually new or existing investors).
- **Settlement:** Funds are transferred to the sellers, typically within 7–10 business days, minus any applicable fees or taxes.
- **Tax Reporting:** Shareholders receive relevant tax forms (e.g., Form 1099-B) for income reporting.

Legal and Regulatory Considerations

Securities Law Compliance

Offers must comply with SEC regulations, including the Securities Exchange Act of 1934 and exemptions under Rule 144 or Regulation D.

ERISA and Tax Implications

Special considerations apply for shares held in retirement plans.

Company Governance

Board approval, right of first refusal (ROFR), and investor rights agreements (IRAs) must be navigated.

Case Studies and Market Trends

- **Gusto**, the HR tech company, is currently conducting a tender offer, allowing eligible employees to sell a portion of their company shares.
- **Stripe** conducted a \$6.5B secondary round including employee liquidity in 2023.
- **Databricks** and **SpaceX** regularly structure tender offers to manage cap table and attract talent.
- Increasing repeat transactions indicate growing normalization of private market liquidity.

What We Recommend

- Engage with legal, tax, and financial advisors early.
- Work with a financial advisor that understands your full financial picture and has experience in private market transactions.
- Use a reputable platform with compliance infrastructure.

Conclusion

Tender offers through private exchanges may offer a powerful solution to the liquidity conundrum faced by employees of and early investors in private companies whose valuations have increased considerably. With proper planning, regulatory diligence, and strategic execution, companies can provide meaningful liquidity while preserving long-term alignment, and individuals can more efficiently and effectively manage and plan around the wealth created by these enterprises.

PUREfi Wealth advisors have decades of experience working with founders, executives, and other stakeholders of both public and private entities to implement strategies around the concentrated wealth created through company stock.

We can help!

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