Regulating Pre-IPO Secondary Trading: Rule 144, Reg D and the Solicitation Line

How the US framework governs who may sell a private share, who may buy it, and where the line falls between a permitted resale and an unlawful distribution

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ABSTRACT

Abstract. A pre-IPO secondary trade looks, to the parties, like a simple sale: a holder of private shares wants to sell, a buyer wants to own them, and a price is agreed. Underneath that simplicity sits a dense body of United States securities law that governs whether the sale is lawful at all. The shares were issued under an exemption from registration, almost always Regulation D, and they remain restricted securities in the buyer's hands. Their resale therefore needs its own exemption, and the way the deal is marketed, the way the buyer's status is checked, and the way the shares are delivered all sit inside rules that carry real consequences when they are crossed. This paper maps that framework for the two parties who must live inside it every day: the intermediaries who source, structure and syndicate these trades, and the family offices and ultra-high-net-worth buyers who acquire the shares. It treats three questions as the spine of the analysis. First, may this holder sell, which is governed by Rule 144 and the holding period and the doctrine that has come to be called Section 4(a)(1.5). Second, may this person buy, which is governed by the accredited-investor, qualified-purchaser and qualified-institutional-buyer definitions. Third, how was the deal offered, which turns on the line between a private placement and a general solicitation, and on the difference between Rule 506(b) and Rule 506(c). The paper argues that the regulatory question is not a back-office formality to be cleared after the price is agreed but the first filter through which any deal should pass, because a trade that fails it is not a cheap trade, it is a void or unlawful one. It is calibrated for the Gulf participant who reaches a US private market from outside it, and for whom the framework is most usefully read as a set of gates rather than a set of forms. The paper is educational and analytical. It is not legal advice, it is not investment advice, and it makes no recommendation about any security, structure or transaction. The figures are illustrative and the calibrations are stylised.

JEL Classification: G18, G24, G28, K22, G23, D82

Keywords: pre-IPO secondaries, Rule 144, Regulation D, Rule 506, general solicitation, Section 4(a)(1.5), accredited investor, qualified purchaser, private markets, intermediaries

1. INTRODUCTION

A pre-IPO secondary trade is presented to its parties as a transaction in an asset. A holder of shares in a late-stage private company wishes to sell. A buyer wishes to own those shares before the company lists. An intermediary introduces the two, a price is struck against the company's last financing round, and the deal closes. Described in those terms, the transaction is indistinguishable from the sale of any other private asset, and the only questions that seem to matter are the price, the discount and the quality of the company. That framing is comfortable, and it is wrong.

It is wrong because the share being sold is not an ordinary asset. It is a restricted security, issued by a company that never registered it with the United States Securities and Exchange Commission and that relied instead on an exemption from registration to issue it in the first place. The most common such exemption is Regulation D, and in particular Rule 506, under which the great majority of venture-backed companies raise their private capital. A security issued under that exemption carries its restriction with it. It does not become freely tradeable simply because a willing buyer appears. Its resale needs its own justification in law, and the absence of that justification does not make the trade expensive or awkward. It makes it unlawful, and in the worst case it makes it void, unwinding the buyer's title and exposing the seller and the intermediary to liability.

This is the central claim of the paper. In a pre-IPO secondary, the regulatory question is not a compliance formality to be cleared by the lawyers after the commercial terms are agreed. It is the first and most consequential filter through which the deal must pass, because it determines whether there is a deal at all. A buyer who has negotiated a brilliant discount on a position that cannot lawfully be sold to them has negotiated nothing. An intermediary who has built a syndicate around a holder who is not yet free to sell has built a liability. The discipline this paper urges is to place the regulatory test first, ahead of price, and to treat it as a sequence of gates that the trade either passes or does not.

The framework has three gates, and they answer three different questions about the same trade. The first asks whether the holder may sell. A restricted security cannot simply be resold by its owner; the owner needs a resale exemption, and the principal route is Rule 144, which imposes a holding period and, for some sellers, volume and manner-of-sale constraints. Where Rule 144 is unavailable, a body of practice that the market calls Section 4(a)(1.5) provides a private resale route between sophisticated parties. The second gate asks whether this particular person may buy. Private securities may be sold only to investors who meet defined thresholds, and the thresholds matter because they determine which structures are open: the accredited-investor test for Regulation D, the qualified-purchaser test for larger pooled vehicles, and the qualified-institutional-buyer test for the Rule 144A market. The third gate asks how the deal was offered. A trade marketed quietly to known, sophisticated counterparties is a private placement. A trade advertised to the world is a general solicitation, and the moment it crosses that line the rules that apply to it change, the verification burden rises, and a misstep can destroy the exemption the whole structure relies upon.

The paper is written for two readers, and they sit on opposite sides of the same trade. The first is the intermediary: the broker, the investment banker or the platform that sources late-stage private shares, structures the vehicle that holds them and syndicates the position to buyers. For the intermediary the framework is a description of the perimeter inside which a business must operate, and the cost of leaving that perimeter is measured in rescinded trades, regulatory action and reputational damage. The second reader is the buyer: the family office or ultra-high-net-worth investor who is offered a position and must decide not only whether it is good value but whether it can lawfully and cleanly be owned. For the buyer the framework is a checklist of conditions that, if unmet, mean the asset they think they are buying is not the asset they will receive.

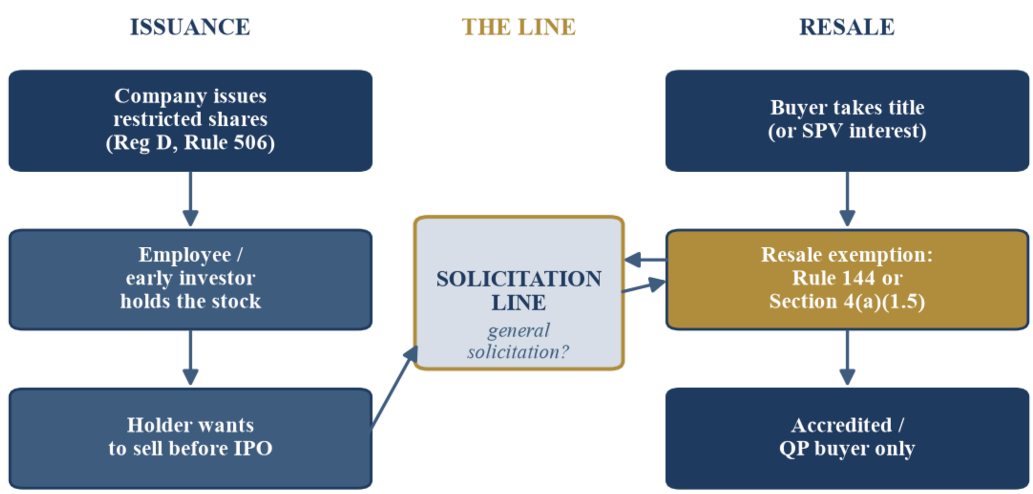
The calibration of the paper reflects a particular vantage point. The Gulf participant reaches the United States private market from outside it. The family offices of the region are among the most active new buyers of US late-stage private shares, and the intermediaries who serve them increasingly co-broke into US deal flow. Yet the framework that governs those trades is foreign to the jurisdictions in which these parties are domiciled, and the instinct to treat a share sale as a matter of contract rather than of securities regulation is strong. The paper therefore reads the framework as a set of gates that a non-US party can apply from first principles, rather than as a catalogue of forms that presumes a US compliance function already exists.

Three caveats frame everything that follows. First, this is an educational and analytical document. It is not legal advice, it is not investment advice, and nothing in it should be read as a recommendation to buy, sell or structure any security or transaction. The law it describes is summarised for orientation and is not a substitute for advice from qualified US securities counsel on a specific deal. Second, the law in this area is detailed, fact-specific and subject to change, and the descriptions here are deliberately stylised to make the structure legible rather than to capture every exception. Third, the figures and tables are illustrative. They are schematics and stylised calibrations designed to make the mechanism visible, not data, forecasts or representations about any market or security.

The paper makes four contributions. First, it organises a dispersed body of rules into three sequential gates, sell, buy and offer, that a non-specialist can apply in order. Second, it draws the single most consequential and least understood line in the framework, the solicitation line between Rule 506(b) and Rule 506(c), and shows why crossing it changes the verification burden. Third, it connects the regulatory gates to the deal structures the market actually uses, the direct sale, the single-asset special-purpose vehicle, the forward and the Rule 144A block, and shows how each structure sits differently against the rules. Fourth, it provides the intermediary and the buyer with practical instruments: a compliance funnel, a checklist and a red-flag list calibrated for the cross-border buyer.

The remainder of the paper is organised as follows. Section 2 reviews the legal and economic literature on registration, exemption and the regulation of resale, and sets out five propositions. Section 3 describes the analytical method and states the stylised assumptions behind the figures. Section 4 presents the framework itself, gate by gate. Section 5 maps the gates onto the deal structures the market uses and onto the cross-border buyer's position. Section 6 discusses the limitations of the analysis. Section 7 concludes. Four appendices provide the base-case assumptions, a compliance checklist, a red-flag list and a glossary.

Figure 1. The Regulatory Path of a Pre-IPO Secondary Share



Illustrative schematic. A restricted share issued under Regulation D must pass through a resale exemption and a solicitation test before it can lawfully reach an eligible buyer. Each box is a condition the trade must satisfy, not a step that can be assumed.

2. REGULATORY BACKGROUND AND PROPOSITIONS

The framework draws on five bodies of work: the rationale for securities registration and the design of exemptions; the law and practice of restricted-security resale; the definition of investor eligibility; the regulation of how private offerings may be marketed; and the economics of information asymmetry that underlies all of it. This section reviews each in turn and distils the framework into five propositions that the rest of the paper develops.

2.1 Registration, Exemption and the Logic of the Restricted Security

The foundational instrument is the Securities Act of 1933, which makes it unlawful to offer or sell a security in the United States unless the sale is registered with the Commission or qualifies for an exemption from registration. Registration is the public-market regime: the apparatus of prospectuses, audited financials and continuous disclosure that surrounds a listed company. It is expensive, slow and designed for companies that intend to sell to the public at large. A private company raising capital from a handful of sophisticated investors does not register; it relies on an exemption, and the exemption most companies use is Section 4(a)(2), the private-placement exemption, as elaborated by the safe harbour of Regulation D and within it Rule 506.

The logic of the exemption explains the restriction that follows. The exemption is granted because the buyers are sophisticated and the offering is private, so the protective machinery of registration is not needed. If the buyer could immediately resell the shares into the public market, the exemption would become a back door around registration: a company could place shares privately with a friendly buyer who then distributed them to the public, achieving an unregistered public offering in two steps. To prevent this, securities sold under the private-placement exemption are restricted securities. They carry a legend, they cannot be freely resold, and their resale requires its own exemption. The restriction is not an accident of the rules; it is the mechanism that makes the issuance exemption coherent.

This is the first thing the secondary-market participant must internalise. The share they are buying or selling is restricted by design. The restriction travels with the security into the buyer's hands, and the buyer in turn becomes a holder who cannot freely resell. A pre-IPO secondary is therefore not the trade of a free asset; it is the controlled transfer of a restricted one, and the control is the subject of the next literature.

2.2 Resale of Restricted Securities: Rule 144 and Section 4(a)(1.5)

Because a restricted security cannot be freely resold, the law provides routes by which it may lawfully change hands. The principal route is Rule 144, a safe harbour that allows a holder to resell restricted securities once defined conditions are met. The central condition is a holding period: the seller must have held and fully paid for the securities for a minimum period, six months for the securities of a reporting company and twelve months for a non-reporting company, which describes most private issuers. The holding period exists to demonstrate that the seller took investment risk rather than acting as a conduit for distribution.

Rule 144 then distinguishes between two kinds of seller. A non-affiliate, an ordinary holder with no control relationship to the company, who has satisfied the holding period may generally resell without volume limits or manner-of-sale constraints, subject to the availability of current public information for reporting companies. An affiliate, typically an officer, director or large holder, faces continuing constraints even after the holding period: volume limitations that cap how much may be sold in a given window, manner-of-sale requirements, and a notice filing. For private-company secondaries the affiliate distinction matters enormously, because founders and early executives are often affiliates, and their shares cannot be sold as freely as those of an early employee or angel.

Where Rule 144 is unavailable, for example because the holding period is not met or the company's information is not current, the market relies on a second route. This is the resale analogue of the private-placement exemption, a private resale from one sophisticated holder to another that does not involve a public distribution. Practitioners came to call this the Section 4(1.5) exemption, a shorthand that the 2012 reforms codified in substance as Section 4(a)(7), and it is now widely referred to as Section 4(a)(1.5). Under it a restricted security may be resold privately to an accredited investor provided the transaction is not a public offering and certain information is available. It is slower and more documentation-heavy than a clean Rule 144 sale, and it is the workhorse of the pre-IPO secondary market precisely because so many sellers cannot satisfy Rule 144.

2.3 Who May Buy: Accredited Investors, Qualified Purchasers and QIBs

A private security may not be sold to anyone. The buyer must meet an eligibility threshold, and the framework defines several, each opening a different set of doors. The most basic is the accredited investor, defined in Regulation D by income, net worth or, since the 2020 amendments, by professional certification. An individual generally qualifies through income above a threshold sustained over two years, or net worth above a threshold excluding the primary residence, or by holding certain professional licences. Entities qualify through asset size or because all their equity owners are accredited. The accredited-investor test is the gate to Regulation D itself: a Rule 506 offering may include non-accredited investors only in limited numbers and with heavy disclosure, so in practice the market sells almost exclusively to accredited buyers.

Above the accredited investor sits the qualified purchaser, defined in the Investment Company Act, generally an individual or family entity owning a large amount in investments. The qualified-purchaser test matters because it determines which pooled vehicle a buyer may enter. A fund relying on the 3(c)(7) exclusion may admit only qualified purchasers but may have an unlimited number of them, whereas a 3(c)(1) fund may admit accredited investors but is capped in number. Single-asset special-purpose vehicles, the workhorses of pre-IPO syndication, are typically built around one of these exclusions, so the buyer's status determines which vehicle can be offered to them.

Highest of all sits the qualified institutional buyer, an institution that owns and invests a very large amount in securities. The qualified-institutional-buyer definition is the gate to the Rule 144A market, in which large blocks of restricted securities trade among institutions free of the holding-period and volume constraints that bind ordinary resales. Rule 144A is mostly a debt-market mechanism, but for the largest pre-IPO blocks it is the channel through which institutional buyers transact, and the family office that aspires to that channel must understand the threshold that admits it.

Figure 2. The Eligibility Ladder: Who May Buy What

Illustrative. The buyer's status determines not only whether they may participate but which structures are open to them. Thresholds are described in general terms and are not the precise statutory figures, which change and should be confirmed with counsel.

2.4 The Marketing of Private Offerings and the Solicitation Line

How a private offering is marketed is as tightly regulated as who may buy it. The historic premise of the private-placement exemption was that the offering was private, meaning it was not advertised to the public but offered to a limited circle of investors with whom the issuer or its agents had a pre-existing, substantive relationship. Advertising a private offering, a general solicitation, was treated as inconsistent with the exemption, because an offering broadcast to the world looks like a public offering and ought to be registered as one.

The JOBS Act of 2012 changed this in a specific and important way. It created Rule 506(c), which permits general solicitation of a private offering, lifting the historic prohibition on advertising, but on a strict condition: every purchaser must be an accredited investor, and the issuer must take reasonable steps to verify that status rather than relying on the buyer's self-certification. The older Rule 506(b) remains available for those who do not solicit generally; under it the issuer may rely on the buyer's representation of accredited status and may include a limited number of sophisticated non-accredited investors. The two rules thus mark out a line. On one side, quiet, relationship-led syndication under 506(b), with a lighter verification burden. On the other, open marketing under 506(c), with a heavier one. The line between them is the single most consequential boundary in the secondary-market framework, because crossing it inadvertently, by marketing a 506(b) deal too widely, can destroy the exemption the whole transaction relies upon.

For the intermediary this line is the centre of the compliance discipline. A platform that lists deals openly, that advertises returns, or that markets to a broad list of prospects with whom it has no substantive relationship is on the 506(c) side of the line whether it intends to be or not, and it must then verify every buyer's accredited status. An intermediary that works a quiet book of known relationships may remain on the 506(b) side, but only so long as its marketing genuinely stays private. The line is not drawn by intention; it is drawn by conduct.

2.5 Information Asymmetry and the Function of the Rules

Beneath the specific rules sits an economic rationale that helps the non-specialist read them as a coherent system rather than a list of obstacles. The classic analysis of markets with asymmetric information shows that when sellers know more than buyers, and buyers cannot tell good assets from bad, the market can unravel: buyers discount everything to protect against the worst case, good sellers withdraw, and quality declines. Securities regulation is, in large part, a response to this problem. Registration forces disclosure so that public buyers are not at an informational disadvantage. Exemptions are granted where the buyers are sophisticated enough to protect themselves, which is why eligibility thresholds exist. The solicitation rules limit who may be approached so that unsophisticated buyers are not drawn into offerings designed for professionals.

Read this way, the three gates of the framework are not arbitrary. The resale rules ensure the seller is a genuine investor and not a conduit. The eligibility rules ensure the buyer can bear and assess the risk. The solicitation rules ensure the offering reaches only those it was meant for. Each gate addresses a different facet of the same underlying problem, that private securities trade without the protective disclosure of public markets, and the system tolerates that absence only when the parties and the process are constrained in ways that substitute for it.

2.6 Synthesis and Propositions

Taken together, these literatures imply that a pre-IPO secondary should be approached not as a negotiation over price but as a sequence of regulatory tests, each of which can stop the trade, and only after which price becomes meaningful. The framework reduces to five propositions.

Proposition 1. The regulatory test comes before the price. A trade that cannot lawfully be done has no price worth negotiating, so the gates on selling, buying and offering should be cleared before commercial terms are agreed, not after.

Proposition 2. A restricted security needs a resale exemption, and its availability is a question of fact about the seller. Whether the holding period is met, whether the seller is an affiliate, and whether Rule 144 or Section 4(a)(1.5) applies are determined by the seller's history and status, not by the buyer's wishes.

Proposition 3. The buyer's status determines the structure, not merely the permission. Accredited, qualified-purchaser and qualified-institutional-buyer thresholds decide which vehicles and channels are open, so the buyer's status must be established before the structure is chosen.

Proposition 4. The solicitation line is drawn by conduct, not intention. Whether an offering is a private placement or a general solicitation depends on how it was actually marketed, and crossing the line silently converts a 506(b) deal into one that requires 506(c) verification or loses its exemption.

Proposition 5. The cross-border buyer inherits the US framework in full. A non-US buyer of a US restricted security does not escape the rules by being foreign; the security remains restricted, the resale exemption is still required, and the buyer's own home-jurisdiction rules apply on top, not instead.

3. METHOD AND ASSUMPTIONS

This study is analytical and descriptive rather than empirical. It builds a structured method for reasoning about the legality and structure of a pre-IPO secondary, and it illustrates that method with stylised figures. It does not estimate market sizes, returns or default rates, and it makes no empirical claims about any market or security.

3.1 The Three-Gate Framework

The method organises the framework into three sequential gates, applied in order. Gate one, the sell gate, asks whether the holder may lawfully resell: it tests the holding period, the seller's affiliate status, and the availability of Rule 144 or Section 4(a)(1.5). Gate two, the buy gate, asks whether this person may acquire the security and through which structure: it tests accredited, qualified-purchaser and qualified-institutional-buyer status. Gate three, the offer gate, asks how the deal was marketed and therefore which solicitation regime applies: it tests whether the offering stayed private under 506(b) or crossed into 506(c). A trade must pass all three. Failure at any gate stops the trade or forces it into a different and usually costlier structure.

3.1a What the Framework Does and Does Not Do

The framework is a tool for reasoning about whether and how a trade can lawfully be done. It is not a legal opinion, and it does not replace the role of US securities counsel, who must be engaged on any live transaction. Its purpose is to let an intermediary or a buyer identify the questions that matter early, screen out trades that cannot pass, and arrive at counsel with the right issues already framed. It deliberately simplifies. It states thresholds in general terms rather than precise figures, because the figures change and because the point is the structure rather than the number. It omits exceptions and special cases that a specialist would consider, because including them would obscure the gates that the non-specialist most needs to see.

The choice of an analytical, illustrative method rather than an empirical one is deliberate and follows the subject. The legality of a trade is not a statistical question; it is a question of whether specific conditions are met. The right tool is therefore a decision structure, not a dataset, and the figures in this paper are schematics and stylised calibrations that make that structure visible rather than measurements of anything in the world.

3.2 Assumptions and Their Justification

The stylised inputs used in the figures, the length of the holding period shown, the proportion of enquiries that survive each gate in the compliance funnel, and the relative friction and enforcement indices attached to each deal structure, are illustrative calibrations chosen to make the method legible. They are not forecasts, sourced data points or representations about any market. Table 1 records the base-case assumptions so that the reader can see exactly what has been assumed and vary it. A reader who believes a different calibration is more realistic can substitute it; the structure of the framework is unaffected, which is the point of separating the method from the numbers.

Table 1. Base-Case Assumptions for the Three-Gate Framework

Parameter	Illustrative value	Rationale
Holding period, non-reporting issuer	12 months	Most private issuers are non-reporting
Holding period, reporting issuer	6 months	Shorter where current information exists
Affiliate volume cap (window)	Capped, recurring	Affiliates never fully free under 144
Enquiries surviving title check	72 of 100	Chain-of-title gaps are common
Surviving resale-exemption test	55 of 100	Holding period / 4(a)(1.5) failures
Surviving buyer-eligibility test	38 of 100	Channel-specific verification
Surviving transfer-restriction test	27 of 100	ROFR and consent rights bite
Closeable, compliant deals	19 of 100	The compliant residue

Parameter	Illustrative value	Rationale
Highest-friction structure	Forward / allocation	No present title; counterparty risk
Lowest-friction structure	Issuer-led tender	Company controls the process

Indicative, illustrative calibrations used to make the method legible; not forecasts, sourced data or legal thresholds. Statutory figures change and must be confirmed with counsel.

4. THE THREE GATES IN DETAIL

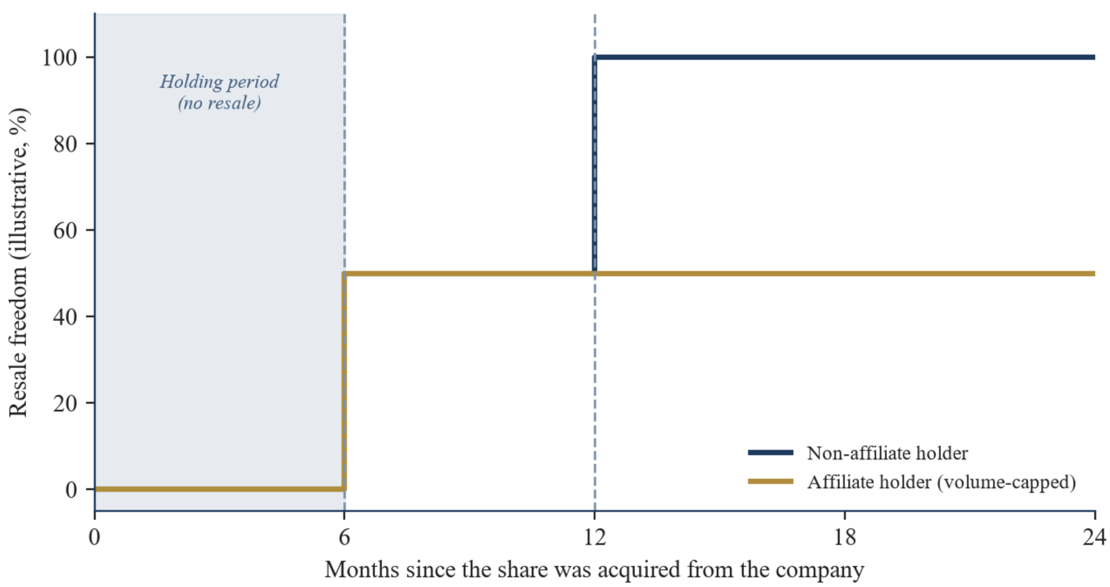
This section works through the three gates in the order a participant should apply them. It begins with the sell gate, because if the holder cannot lawfully sell there is nothing to buy; moves to the buy gate, because the buyer's status shapes the structure; and ends with the offer gate, because how the deal is marketed governs which regime applies to the whole.

4.1 Gate One: May the Holder Sell?

The first gate tests the seller. A restricted security in the seller's hands cannot be resold without an exemption, and the gate establishes which exemption, if any, is available. The analysis has three parts: the holding period, the seller's affiliate status, and the fallback route where Rule 144 does not apply.

The holding period is the threshold question. The seller must have held and fully paid for the securities for the required period, measured from the date the securities were acquired from the company or an affiliate. For the non-reporting private companies that dominate the pre-IPO market the period is the longer one. A seller who acquired shares recently, for instance an employee who exercised options weeks ago or an investor who bought into the last round, has not satisfied it and cannot use Rule 144. This is a frequent and underappreciated point of failure: the most eager sellers are often the most recently arrived, and they are precisely the ones who cannot yet sell.

Figure 3. How Resale Freedom Opens Over Time Under Rule 144



Illustrative. A non-affiliate holder moves from no resale, through a constrained window, to substantially free resale as the holding period elapses, while an affiliate remains volume-capped indefinitely. The widths and timings are stylised, not statutory.

The second part is the seller's status. A non-affiliate who has cleared the holding period is largely free, subject for reporting companies to the availability of current public information. An affiliate is never fully free: even after the holding period, the affiliate faces volume limits that cap the quantity sold in a given window, manner-of-sale conditions, and a notice filing. In private-company secondaries this distinction is decisive, because the largest and most sought-after blocks are often held by founders and senior executives who are affiliates. A buyer who is offered a founder's block must understand that the block cannot be sold as freely as the same number of shares held by an early employee, and that the affiliate constraints shape how, and how quickly, the position can be assembled.

The third part is the fallback. Where Rule 144 is unavailable, because the holding period is not met, because the seller cannot satisfy its conditions, or because current information is lacking, the trade does not necessarily fail. It can proceed under the private-resale route the market calls Section 4(a)(1.5), under which a restricted security is resold privately to an accredited investor in a transaction that is not a public offering. This route carries a heavier documentation burden, a representation letter, a confirmation that the buyer is accredited, and an absence of general solicitation, but it is the route through which much of the pre-IPO market actually clears, because so many of its sellers cannot satisfy Rule 144. The practical consequence is that the sell gate is rarely a simple yes or no; it is a determination of which route applies and therefore of how much friction the trade carries.

4.2 Gate Two: May This Person Buy, and Through What?

The second gate tests the buyer. It establishes not merely whether the buyer is permitted to participate but which structures are open to them, because the eligibility thresholds map onto the vehicles the market uses. The gate has three rungs, and a buyer sits on one of them.

The base rung is the accredited investor. Almost every pre-IPO secondary is sold only to accredited buyers, because a Rule 506 offering that admits non-accredited investors triggers heavy disclosure and is rarely worth the burden. For an individual, accreditation generally rests on income sustained over two years, on net worth excluding the primary residence, or on holding certain professional qualifications. For an entity it rests on asset size or on all owners being accredited. A family office structured as an entity will usually qualify comfortably, but the test must be established for the specific buying entity, not assumed from the family's wealth in the abstract.

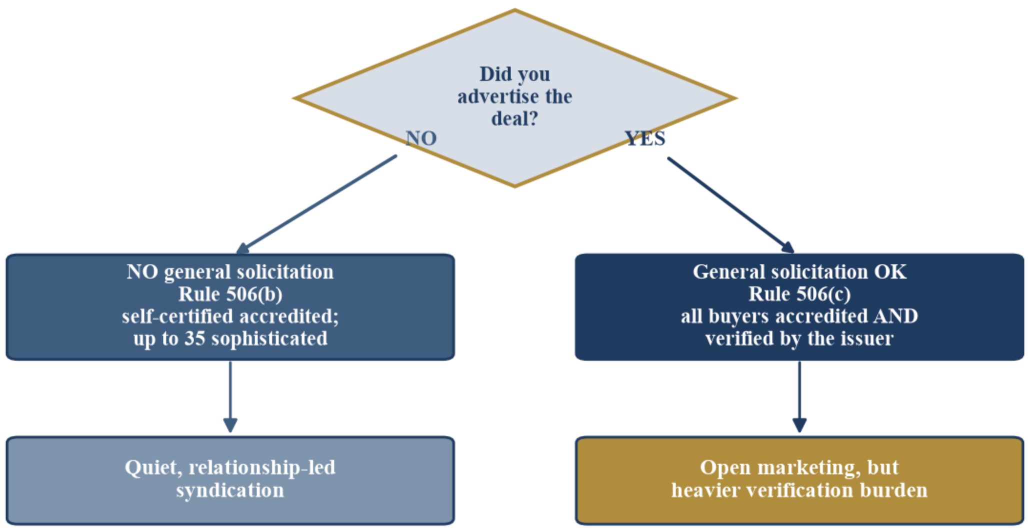
The middle rung is the qualified purchaser, and it governs access to pooled vehicles. A single-asset special-purpose vehicle, the structure through which most syndicated pre-IPO positions are held, relies on an exclusion from the Investment Company Act. If it relies on the 3(c)(7) exclusion it may admit only qualified purchasers, but it may admit an unlimited number of them, which is why larger syndications favour it. If it relies on the 3(c)(1) exclusion it may admit accredited investors who are not qualified purchasers, but it is capped in the number of beneficial owners. A buyer who is accredited but not a qualified purchaser can enter a 3(c)(1) vehicle but not a 3(c)(7) one, and a syndicator building a vehicle must know the status of its investors before choosing the exclusion. The buyer's status, in other words, is not just a permission; it determines the architecture of the deal.

The top rung is the qualified institutional buyer, which governs the Rule 144A market in which the largest blocks of restricted securities trade among institutions. Most family offices will not meet the qualified-institutional-buyer threshold, and the rung is included here not because most buyers reach it but because the largest and most sophisticated do, and because understanding it clarifies why certain deal flow is visible only to the very largest institutions. The eligibility ladder is cumulative: each rung opens everything below it and one channel above.

4.3 Gate Three: How Was the Deal Offered?

The third gate tests the offering itself, and it is the gate that most often catches the intermediary unawares, because it turns not on the parties' status but on their conduct. The question is whether the deal was marketed as a private placement or as a general solicitation, and the answer determines which regime governs the whole transaction.

Figure 4. The Solicitation Line: Rule 506(b) Versus Rule 506(c)



Illustrative decision schematic. Whether the deal was advertised, rather than whether the parties intended it to be private, determines which rule applies and how heavily buyers must be verified.

On one side of the line sits Rule 506(b), the quiet route. Under it the offering is not advertised; it is taken to investors with whom the issuer or its intermediary has a pre-existing, substantive relationship. The issuer may rely on the buyer's own representation that they are accredited, and may include a small number of sophisticated non-accredited investors. The verification burden is light, but the marketing must genuinely stay private. The moment the deal is advertised, posted on an open platform, sent to a broad list of strangers, or pitched at a public forum, it has been generally solicited, and 506(b) is no longer available to it.

On the other side sits Rule 506(c), the route the JOBS Act created. It permits general solicitation, so the deal may be advertised, but it imposes a strict price: every purchaser must be an accredited investor, and the issuer must take reasonable steps to verify that status, through documents such as tax filings, financial statements or third-party confirmations, rather than relying on the buyer's word. The trade-off is symmetrical. 506(b) offers light verification but demands marketing discipline; 506(c) offers marketing freedom but demands rigorous verification. The danger lies in drifting from one to the other without realising it: an intermediary that believes it is running a 506(b) deal but markets it like a 506(c) deal has the worst of both, a general solicitation without the verification that would make it lawful, and an exemption that may be lost.

For the intermediary the practical discipline is to decide, at the outset, which side of the line the deal will sit on and to build the process accordingly. A relationship-led syndicator should document the pre-existing relationships that keep it within 506(b) and should resist the temptation to widen the list. A platform that markets openly should accept that it is a 506(c) operation and should build the verification machinery that 506(c) requires. What no intermediary can safely do is straddle the line.

It is worth being precise about what counts as a pre-existing, substantive relationship, because it is the load-bearing concept on the 506(b) side and it is frequently overstated. A relationship is pre-existing if it was formed before the particular offering was contemplated, and it is substantive if the intermediary has enough information about the prospect to form a reasonable belief that they are sophisticated and, where relevant, accredited. A name on a marketing list, a contact met at the conference where the deal was pitched, or a prospect added the week the deal launched is none of these things. The discipline that keeps an intermediary safely within 506(b) is therefore unglamorous: it is the patient accumulation of genuine relationships ahead of any specific deal, recorded well enough that the claim can be defended later. Intermediaries who try to manufacture the relationship retrospectively, after marketing widely, find that the record does not support them.

Table 2. Rule 506(b) Versus Rule 506(c): The Two Sides of the Solicitation Line

Dimension	Rule 506(b)	Rule 506(c)
Marketing	No general solicitation; private only	General solicitation permitted
Permitted buyers	Accredited plus limited sophisticated	Accredited investors only
Verification of status	Buyer's representation may suffice	Issuer must take reasonable steps to verify
Relationship required	Pre-existing, substantive relationship	Not required; deal may be advertised
Verification burden	Lighter	Heavier and documented
Typical user	Relationship-led syndicator	Open platform or public campaign
Principal risk	Drifting into solicitation unawares	Inadequate verification of a buyer

Illustrative comparison stated in general terms; not a statement of the precise rule, which should be confirmed with counsel.

5. STRUCTURES, INTERMEDIARIES AND THE CROSS-BORDER BUYER

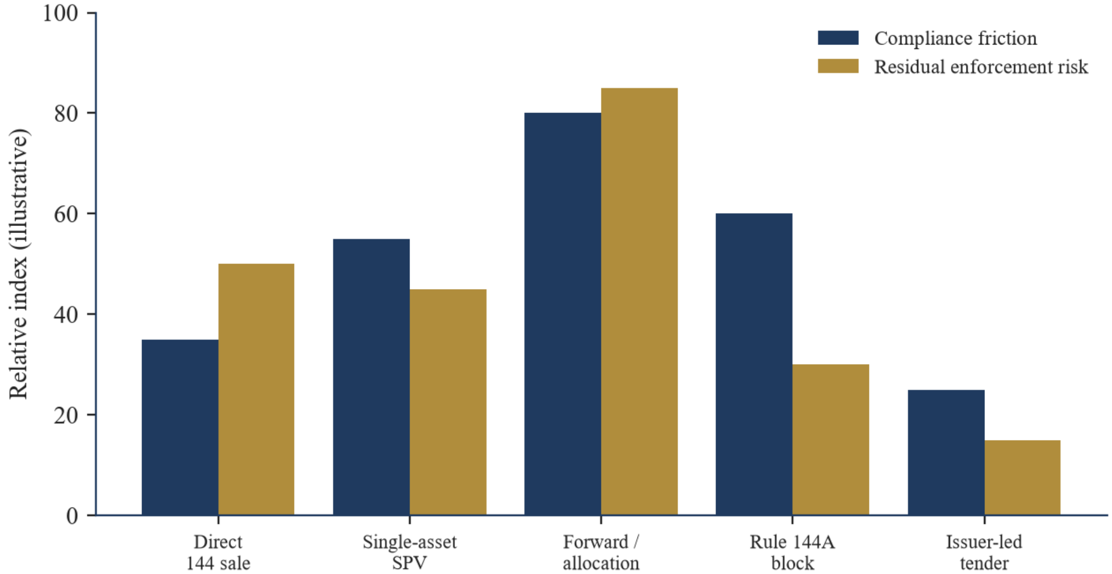
The three gates are abstract until they are mapped onto the structures the market actually uses and onto the position of the participant who reaches the US market from outside it. This section makes both connections.

5.1 How the Gates Sit Against Each Deal Structure

The market clears pre-IPO secondaries through a small number of recurring structures, and each sits differently against the three gates. The direct sale, in which the buyer takes title to the shares from the seller, is the cleanest against the framework but the most exposed to the sell gate, because it depends entirely on the seller's ability to deliver good, transferable title under a valid resale exemption. The single-asset special-purpose vehicle, in which buyers hold an interest in a vehicle that owns the shares, shifts the analysis: the vehicle must itself qualify under an Investment Company Act exclusion, which drives the buyer-eligibility question to the qualified-purchaser rung, and the interests in the vehicle are themselves securities whose offering must respect the solicitation line.

The forward, or allocation, in which the buyer pays now for shares the counterparty does not yet hold, carries the highest friction of all, because there is no present title to test against the sell gate and the buyer is exposed to the counterparty's eventual ability to deliver. It is the structure most likely to disguise a position that would fail the gates if examined directly, and it warrants the most scepticism. The Rule 144A block, available only between qualified institutional buyers, sits outside the ordinary holding-period constraints but is open only to the largest institutions. The issuer-led tender, in which the company itself organises a structured liquidity event, carries the least friction, because the company controls the process, polices its own transfer restrictions and can ensure the gates are cleared, which is why such programmes have become the preferred route for the largest private companies.

Figure 5. Compliance Friction and Residual Risk by Structure

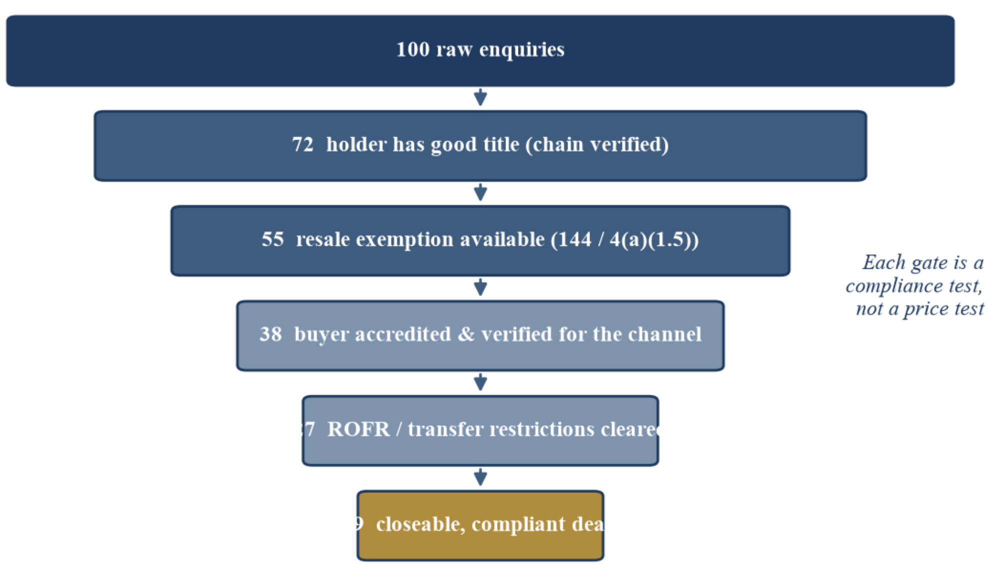


Illustrative indices. The forward carries both the highest compliance friction and the highest residual enforcement risk, while issuer-led tenders sit lowest on both; the values are stylised to convey relative ordering, not measured quantities.

5.2 The Intermediary's Compliance Funnel

For the intermediary, the three gates combine into a funnel through which raw deal flow is filtered down to the trades that can lawfully and cleanly be closed. The funnel is a discipline as much as a diagram: it forces the intermediary to apply the gates in order and to reject, early, the enquiries that cannot survive them, rather than carrying a doubtful deal deep into a process before discovering it fails. The earlier a deal dies, the cheaper its death.

Figure 6. The Intermediary's Compliance Funnel



Illustrative. Of a stylised hundred raw enquiries, only a minority survive title verification, the resale-exemption test, buyer eligibility and transfer-restriction clearance to become closeable, compliant deals. The attrition is illustrative and conveys that most enquiries fail a compliance gate, not a pricing one.

The figure makes the central message of the paper concrete. Most enquiries that reach an intermediary do not fail on price; they fail on a compliance gate. The holder cannot deliver good title, or has not held the shares long enough, or the buyer cannot be verified for the channel, or a right of first refusal or transfer restriction blocks the sale. An intermediary whose process tests price first and compliance last will repeatedly invest effort in deals that were never closeable. An intermediary whose funnel applies the gates first preserves its effort for the trades that can survive.

5.3 The Cross-Border Buyer's Position

The Gulf buyer who acquires a US restricted security occupies a particular and sometimes misunderstood position. The intuition that a foreign buyer somehow sits outside the US framework, that the rules are a domestic American concern, is mistaken and dangerous. The security is a US restricted security regardless of who holds it. Its resale still requires a US exemption. The vehicle through which it is held is still a US securities offering subject to the solicitation line. The buyer's foreignness changes the analysis at the margins, sometimes opening offshore routes such as Regulation S for offerings made outside the United States, but it does not lift the buyer out of the framework when the security and its issuer are American.

On top of the US framework sits the buyer's own home-jurisdiction regime. A family office domiciled in the Gulf must satisfy its local rules on holding foreign securities, on the vehicles it uses, and on any onward distribution to family members or co-investors. These rules apply in addition to, not instead of, the US framework, and the two must be reconciled. The practical implication is that the cross-border buyer needs advice on both sides, and that the intermediary serving such a buyer cannot treat the US analysis as the whole of the compliance question. The clean cross-border deal is one that passes the US gates and the home-jurisdiction gates together, and the structures that achieve this, typically a properly constituted vehicle advised on both sides, are the ones that survive scrutiny.

There is, finally, a reputational dimension that matters more for the cross-border participant than the rulebook alone suggests. A family office building a long-term presence in US private markets, and an intermediary building a durable co-broking relationship with US counterparties, both depend on being seen as clean. A single rescinded trade, a single deal that drew regulatory attention, can close doors that took years to open. The discipline of placing the regulatory test first is therefore not only a matter of avoiding liability on a given trade; it is a matter of preserving access to the market over time. The framework, read this way, is less a constraint than the price of admission to a market worth being admitted to.

5.4 Who Holds the Verification Burden, and Why It Travels

A point that the gate-by-gate analysis can obscure is that the duties created by the framework do not rest on a single party. They travel along the chain, and a participant who assumes that another party has discharged a duty, without confirming it, inherits the consequence if it was not discharged. The issuer whose shares are being sold has an interest in the resale exemption being valid, because an unlawful resale can taint the issuer's own exemption and complicate a future registration. The seller carries the representations about holding period and title. The intermediary carries the conduct that determines the solicitation regime and, where it acts as a broker, a set of its own registration and suitability obligations. The buyer carries the truth of its own accredited or qualified-purchaser status. No single party can clear all three gates alone, and the clean deal is one in which each party's duty is identified, allocated and documented rather than assumed.

For the intermediary in particular, there is a registration question that sits underneath the three gates and is easy to overlook. A party that is in the business of effecting securities transactions for the account of others, that solicits trades, handles customer funds or securities, or takes transaction-based compensation, may itself need to be a registered broker-dealer. A platform or an individual who arranges pre-IPO secondaries for a fee, believing themselves to be a mere introducer, may in substance be acting as an unregistered broker, and the consequences of that, including the risk that counterparties can unwind trades, are severe. The cross-border intermediary co-broking into US deal flow must understand that the question of whether it needs to be registered, or to work through a registered party, is a precondition to the business, not a detail of a single trade.

This is why the framework is best understood not as a checklist applied once at the point of sale but as a set of standing capabilities a serious participant builds. The intermediary that intends to operate in this market builds the relationships, the documentation and, where needed, the registered status that let it clear the gates as a matter of routine. The buyer that intends to be active builds the verification file, the vehicle and the dual-jurisdiction advisory relationship that let it satisfy the gates without re-litigating them on every trade. The cost of those capabilities is the entry cost of the market, and the participants who treat it as such transact more cleanly, and more cheaply over time, than those who improvise the answer to each gate as it arises.

5.5 What Failure at Each Gate Actually Costs

The argument that the regulatory test should come first rests on the claim that failure is expensive, and it is worth making that cost concrete, because a participant who does not feel the cost will not respect the discipline. Failure at the sell gate, where the holder could not lawfully resell, is the most fundamental. A purported sale of a restricted security without a valid resale exemption is an unlawful, unregistered sale of securities. The buyer may have a right of rescission, the power to unwind the trade and recover the purchase price, which means the buyer who thought they had acquired an asset has instead acquired a claim against a seller who may no longer have the money. The seller and any intermediary face potential liability, and the issuer's own exemption may be drawn into question. None of this is cured by the quality of the company or the attractiveness of the price.

Failure at the buy gate is subtler but no less damaging. A vehicle that admitted an investor who did not meet the threshold its exclusion required, an accredited investor admitted to a 3(c)(7) vehicle reserved for qualified purchasers, for instance, may have lost the exclusion it depended on, with consequences for every investor in the vehicle, not only the ineligible one. A single misjudged admission can therefore contaminate an entire syndication. This is why the buyer-eligibility question is not a courtesy check on one investor but a structural precondition that the syndicator must police for the whole vehicle.

Failure at the offer gate, the inadvertent general solicitation, destroys the exemption the offering relied upon. A deal marketed as a 506(b) private placement but in fact generally solicited has no valid exemption, because it neither stayed private as 506(b) requires nor verified its buyers as 506(c) requires. The result is an unregistered public offering, the gravest characterisation available, carrying rescission rights and regulatory exposure for the issuer and its agents. The asymmetry is cruel: the failure is easy to commit, often through nothing worse than enthusiasm in marketing, and very hard to repair after the fact. The discipline of deciding, in advance, which side of the line the deal sits on, and then behaving accordingly, is the only reliable protection.

These consequences explain the paper's insistence on sequence. Each is a category of harm that no amount of commercial skill can offset, and each is avoidable by a process that tests the gate before the price. The cost of clearing the gates early is a few hours of disciplined analysis and, on a live deal, the fee of competent counsel. The cost of clearing them late, or not at all, is the trade itself. For a participant building a durable presence in this market, that arithmetic is not close.

6. LIMITATIONS AND DISCUSSION

The framework has limits that should be stated plainly. First and most important, it is a structure for reasoning, not a legal opinion. It summarises a complex body of law in simplified terms to make it legible, and that simplification necessarily omits exceptions, special cases and recent developments that a specialist would weigh. No trade should be done on the strength of this paper; every live transaction requires qualified US securities counsel, and where the buyer is cross-border, counsel in the home jurisdiction as well.

Second, the law in this area changes. Thresholds for accredited-investor and qualified-purchaser status have been amended within recent memory and may be amended again. The treatment of general solicitation, the scope of resale exemptions, and the rules governing platforms and intermediaries are all subject to regulatory and legislative revision. The paper deliberately states thresholds in general terms rather than precise figures precisely because the figures move; a reader who relies on a specific number from this paper rather than confirming the current rule has misused it.

Third, the framework is calibrated for the common case and may mislead at the edges. It assumes the typical pattern of a venture-backed company that raised under Rule 506, issued restricted shares to employees and investors, and is now the subject of secondary interest. Companies with unusual capital structures, securities issued under other exemptions, or histories that complicate the chain of title may not fit the pattern, and the gates may need to be applied differently. The framework is a starting point for analysis, not a substitute for it.

Fourth, the figures are illustrative throughout. The holding periods shown, the attrition rates in the compliance funnel, and the friction and risk indices attached to each structure are stylised to convey structure and relative ordering, not to measure anything. They should be read as schematics. A reader who treats the nineteen-in-a-hundred survival rate in the funnel, or the index values in the structure comparison, as empirical findings has read the figures against their stated purpose.

Fifth, the framework addresses legality and structure but not, except in passing, two adjacent questions that any real participant must also answer: whether the price is fair, and whether the underlying company is a good investment. A trade can pass all three gates cleanly and still be a poor decision because the position is overpriced or the company is weak. The gates establish that the trade can lawfully be done and how; they do not establish that it should be. A companion analysis on pricing, marks and diligence is the proper home for those questions, and the present paper should be read as one input into a wider decision rather than as the whole of it.

Despite these limits, the framework earns its place. The most common and most expensive errors in pre-IPO secondary trading are not errors of price; they are errors of legality, made by parties who treated a securities transaction as a contract for an asset and discovered too late that the asset could not lawfully be transferred to them. A structure that places the regulatory test first, that applies the three gates in order, and that rejects early the trades that cannot pass, prevents the category of error that does the most damage. That is a modest claim, but it is the right one, and it is enough.

7. CONCLUSION

A pre-IPO secondary trade is a securities transaction wearing the clothes of an asset sale. The share at its centre is a restricted security, issued under an exemption from registration and carrying that restriction into every hand it passes through. Whether it can lawfully be sold, who may lawfully buy it, and how the deal may lawfully be offered are not formalities to be cleared after the price is agreed; they are the conditions that determine whether there is a trade at all.

This paper has organised the governing framework into three gates. The sell gate asks whether the holder may resell, and answers through the holding period, the affiliate distinction, and the choice between Rule 144 and the private-resale route the market calls Section 4(a)(1.5). The buy gate asks whether this person may acquire the security and through what structure, and answers through the accredited-investor, qualified-purchaser and qualified-institutional-buyer thresholds that decide which vehicles are open. The offer gate asks how the deal was marketed, and answers through the solicitation line between the quiet route of Rule 506(b) and the advertised route of Rule 506(c), a line drawn by conduct rather than intention and crossed at the cost of the exemption itself.

For the intermediary, the framework is a funnel that filters raw deal flow down to the trades that can lawfully close, and the discipline it demands is to apply the gates first and price last, because most enquiries fail a compliance gate rather than a pricing one. For the buyer, and especially for the cross-border buyer who reaches the US market from outside it, the framework is the price of clean, durable access to a market worth being admitted to: the security remains American however foreign its owner, the US gates apply in full, and the home-jurisdiction rules apply on top.

The single discipline that the paper urges is to put the regulatory test first. A brilliant price on a position that cannot lawfully be sold to you is not a bargain; it is a liability dressed as one. The participant who internalises that the regulatory question precedes the commercial one, and who works the three gates in order before negotiating terms, will avoid the category of error that does the most damage in this market, and will earn the standing that keeps its doors open. In a market without the protective disclosure of public exchanges, that discipline is not bureaucracy. It is the substitute for the protection that private securities, by design, do not carry.

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APPENDIX A. BASE-CASE ASSUMPTIONS

The illustrative calibrations underlying the figures are collected in Table 1 in Section 3.2. They are stylised to make the method legible and are not forecasts, sourced data or statutory thresholds. The holding periods, eligibility thresholds and resale conditions referred to throughout the paper are described in general terms; the precise figures change over time and must be confirmed with qualified US securities counsel for any specific transaction. Nothing in this appendix or the paper constitutes legal or investment advice.

APPENDIX B. PRE-IPO SECONDARY COMPLIANCE CHECKLIST

The following checklist restates the three gates as a sequence of questions a buyer or intermediary should answer before commercial terms are agreed. It is an aid to reasoning, not a legal opinion, and it does not replace counsel.

- Sell gate: Has the holder held and fully paid for the shares for the required period?
- Sell gate: Is the seller an affiliate, and if so, what volume and manner-of-sale constraints apply?
- Sell gate: Is Rule 144 available, or must the trade proceed under Section 4(a)(1.5)?
- Sell gate: Can the seller evidence a clean chain of title from the issuer's register to the present holder?
- Buy gate: Is the buying entity an accredited investor, evidenced for that specific entity?
- Buy gate: Is the buyer a qualified purchaser, and is the chosen vehicle relying on 3(c)(1) or 3(c)(7)?
- Buy gate: If a Rule 144A channel is contemplated, does the buyer meet the qualified-institutional-buyer threshold?
- Offer gate: Was the deal marketed privately under 506(b), or generally solicited under 506(c)?
- Offer gate: If 506(c), has every buyer's accredited status been verified, not merely represented?
- Offer gate: Are the pre-existing, substantive relationships supporting a 506(b) claim documented?
- Transfer: Has any right of first refusal, co-sale or company-consent right been cleared in writing?
- Structure: Does the chosen structure (direct, SPV, forward, 144A, tender) fit the parties' status?
- Cross-border: Have the buyer's home-jurisdiction rules been satisfied alongside the US framework?
- Counsel: Has qualified US securities counsel reviewed the specific transaction before closing?

APPENDIX C. RED-FLAG LIST

The following are warning signs that a pre-IPO secondary may fail one of the three gates or may be structured to obscure such a failure. The presence of a flag is not proof of a problem, but it is a reason to slow the trade and to ask harder questions before proceeding.

- The seller acquired the shares recently and cannot evidence the holding period.
- The seller is a founder or senior executive whose affiliate status is not acknowledged.
- The offer is a forward or allocation, a promise of shares the counterparty does not yet hold.
- The deal was found through open advertising yet is presented as a private 506(b) placement.
- The intermediary cannot or will not document the pre-existing relationship that supports a 506(b) claim.
- No verification of the buyer's accredited status is sought despite open marketing.
- The chain of title is incomplete, undocumented or routed through an unexplained intermediary holder.
- A right of first refusal or company-consent right is acknowledged but not yet cleared.
- The structure is unusually complex relative to the size of the position, obscuring who holds title.
- Pressure is applied to close quickly, before counsel can review the resale exemption and the chain.
- The buyer is told that, being foreign, they need not worry about the US rules.

APPENDIX D. GLOSSARY OF KEY TERMS

Restricted security. A security acquired in an unregistered, private transaction that cannot be freely resold without an exemption.

Regulation D / Rule 506. The principal safe harbour under which private companies raise capital without registering the offering.

Rule 144. The safe harbour that allows a holder to resell restricted securities once a holding period and, for affiliates, further conditions are met.

Section 4(a)(1.5). The market shorthand for the private-resale route, codified in substance as Section 4(a)(7), used where Rule 144 is unavailable.

Affiliate. A person in a control relationship with the issuer, such as an officer, director or large holder, who faces continuing resale constraints.

Holding period. The minimum period a holder must have held and paid for restricted securities before Rule 144 resale is available.

Accredited investor. An investor meeting income, net-worth or professional-certification thresholds under Regulation D.

Qualified purchaser. An investor owning a large amount in investments, whose status governs access to 3(c)(7) pooled vehicles.

Qualified institutional buyer. An institution owning and investing a very large amount in securities, eligible for the Rule 144A market.

General solicitation. The advertising or broad marketing of a private offering, which converts it from a 506(b) to a 506(c) regime.

Rule 506(b) / 506(c). The two private-placement routes: quiet marketing with light verification, or general solicitation with strict verification.

Special-purpose vehicle. A company or fund formed to hold a single investment, through which syndicated pre-IPO positions are often held.

Chain of title. The documented sequence of transfers establishing that the seller holds good, transferable title to the shares.

Right of first refusal. A right held by the company or its investors to buy shares before they may be sold to a third party.