ROLE OF A PURCHASER REPRESENTATIVE:

SUPPORTING UNACCREDITED INVESTORS

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Most technology companies raise the capital necessary to develop their technology and business from venture capital investors, business angels, or corporate partners. Usually, these investors are accredited investors, within the meaning of Rule 501 of Regulation D of the Securities Act of 1933.

However, some early investment may come from unaccredited investors, and virtually all venture-backed companies issue stock options to employees that are sooner or later exercised. Most of the employees are not accredited investors.

Accredited Investors

Many companies have non-accredited investors as shareholders. This may raise compliance issues in an acquisition for stock.

Within the meaning of Rule 501, an accredited investor is a natural person with income exceeding $200,000 in each of the two most recent years or joint income with a spouse exceeding $300,000 for those years and a reasonable expectation of the same income level in the current year, or a natural person who has individual net worth, or joint net worth with the person's spouse, that exceeds $1 million at the time of the purchase. California provides for similar provisions regarding a "qualified purchaser".

As IPOs continue to be the exception, the exit route of choice for most companies is a sale to another company in an M&A transaction. As the market rises and stock prices increase, the acquiring company frequently pays with its own stock.

Exempt Transactions

Most often, the stock of the acquiring company is not registered with the SEC, either because the acquirer is a public company that uses newly issued shares that are pending registration, or because the acquirer itself is a private company with restricted stock. Thus, such a stock offering would need to use one of the exemptions provided under Regulation D of the 1933 Securities Act – known as "Reg D Offerings. For very small transactions including only buyers (and seller) in the same states, companies may be able to take advantage of some of the state exemptions, such as California Corporations Code Section 25012.

Usually, the issuance is exempt under Rule 506 of Regulation D, which allows for unlimited amounts of capital raised (Rule 504 limits the sale of securities to $1 million within a 12-month period;

Rule 505 limits the raise to $5 million, also within a 12-month period). Rule 506 also allows the sale to a maximum of 35 non-accredited investors; however, these investors need to be "sophisticated".

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What is "sophisticated"?

In the eyes of the regulators, "sophisticated" means someone who has "either alone or with his purchaser representative(s) such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment." Often, this requirement is fulfilled by retaining a Purchaser Representative.

A purchaser representative may be necessary to comply with securities law when unregistered stock is issued to non-accredited shareholders.

What is a "Purchaser Representative"?

The Purchaser Representative is defined in Rule 501 of the Securities Act.

The purchaser representative "has such knowledge and experience in financial and business matters that he is capable of evaluating, alone, or together with other purchaser representatives of the purchaser, or together with the purchaser, the merits and risks of the prospective investment". The purchaser representative cannot be affiliated with the issuer and needs to be acknowledged by the purchaser in writing.

Armanino regularly acts as purchaser representative, enjoying the opportunity to help unaccredited investors to navigate and understand sometimes complex transactions with hundreds of pages of agreements in a multitude of disclosure documents that today's mergers produce in the interest of compliance and informing investors.

Summary

Purchaser Representatives are regularly retained to help with compliance with securities law to represent non-accredited shareholders in a merger or acquisition where the consideration consists at least partially of restricted stock.

About Armanino[LLP]

Armanino provides an integrated set of accounting services—audit, tax, consulting and technology solutions—to a wide range of organizations operating both in the US and globally. You can count on Armanino to think strategically, to provide the sound insights that lead to positive action. We address not just your compliance issues, but your underlying business challenges, as well—assessing opportunities, weighing risks, and exploring the practical implications of both your short- and long-term decisions. When you work with us, we give you options that are fully aligned with your business strategy. If you need to do more with less, we will implement the technology to automate your business processes. If it's financial, we can show you proven benchmarks and best practices that can add value company-wide. If the issue is operational, we'll consult with your people about workflow efficiencies. If it's compliance, we'll ensure you meet the requirements and proactively plan to take full advantage of the changes at hand. At every stage in your company's lifecycle, we'll help you find the right balance of people, processes, and technology.

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