

Secondary Sales and An Investor Covenant You Don't Want To Miss

If you are investing in early stage companies, there are certain deal terms you want.

Most you probably know already: if it's a round of convertible notes, you want a discount and a cap; if it's a priced round, you want a liquidation preference. Etc.

But there is a new thing you need to add to your list of “must haves.”

You now want your investment documents to include a Section 4(a)(7) covenant.

What the heck is Section 4(a)(7)?

Section 4(a)(7) is a new federal securities law that basically says, it's OK for you to sell your investment in a private company, as long as you don't generally advertise the securities for sale, sell to another accredited investor, and the company cooperates with certain information requirements.

The new federal law trumps state law. So state law won't hold you up.

Unlike the existing resale exemption most commonly used, there is no holding period required under this new law.

What is a Section 4(a)(7) covenant?

This new law is great—but you need the company's assistance to access it, because the law requires the company to provide certain information to the purchaser.

So, get this covenant in your investment documents, and it may be easier for you to later sell your shares.

You can find draft covenants to include in your securities purchase agreements [here](#). Thank you to Bill Carleton (@wac6) and Gary Kocher for collaborating in putting this together.

And if you're a founder or exec, don't despair: Section 4(a)(7) will work for you, too. For a longer, in depth discussion of the new law, see [this article in TechCrunch](#).