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PERSPECTIVE

IPOs: people, planning and critical path items

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Once a company has determined an IPO is the right choice for them and have implemented the necessary steps to prepare for becoming a public company, then the execution stage begins. The key to any successful IPO is people and planning.

People

In the execution stage, the focus will be on the external leadership team who will advise the company through the IPO process. The primary members will include:

- **Underwriting Syndicate.** A reputable investment bank who really understands the company's equity growth story is critical. The reputation and quality of an investment bank's research arm is also an important factor in selection since analysts will cover the company post IPO.

- **Legal Counsel.** In an IPO, legal counsel will act as quarterback and coordinate the entire IPO process from beginning through post-closing. It is important to select legal counsel who is responsive, knowledgeable and process driven to ensure all of the key steps are accomplished.

- **Auditors.** Auditors will be involved before the IPO execution stage even begins and will continue to be involved long after a company has gone public. It is important to select auditors who will be in it with the company for the long haul.

- **Others.** Less visible but important players include the stock exchange, transfer agent and printer. A company's underwriting syndicate or legal counsel can be helpful in the selection process of these players.

Planning

Planning is a good idea for any transaction but in an IPO context, it can mean the difference between success and failure. Legal counsel will put together a comprehensive timeline and can be charged with ensuring each step is executed. It may also be helpful for a company to consider certain critical path items in advance. These items can be categorized into three areas: Corporate Actions, Disclosure & Diligence and Offering Process.

- **Corporate Actions.** Consider early whether any corporate structuring



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actions are necessary, including spin-offs, restructurings or stock splits as the timeline, documentation, financials and disclosure will all need to account for any such actions. It is also important to consider how equity awards will be handled. It is preferable to avoid equity awards entirely during the 12-month period before filing the S-1. The best practice is to grant the equity awards at fair market value to avoid accounting charges and issues under 409A. It is advisable to get third-party valuation reports on a quarterly basis and seek to grant awards based on the most recent valuation report while it is current and maintain strong, consistent documentation.

- **Disclosure & Diligence.** Drafting of the S-1 is the obvious step in execution of an IPO and will continue throughout the execution stage, as well the diligence process but here are a few critical path items to keep in mind:

- **Deal-Breaking Disclosure.** It is important to consider in advance any potential disclosure issues including any pending litigation, contingent liabilities and related party transactions. The S-1 will require disclosure on all of these items so it is important to assess these items up front to determine any deal-breakers.

- **Exhibits.** Companies will have to file material agreements and ordinary course contracts on which their business is "substantially dependent" so it is important to identify them and determine early in the process whether confidential treatment will need to be sought for limited designated portions of such agreements.

- **Consents.** It is important to review all material agreements to determine

if notice, consent and/or waivers are needed prior to filing the registration statement. No company wants to end up with an inadvertent breach in the middle of an IPO process. The other aspect of consents involves the research, industry reports and studies that may be cited throughout the S-1. These citations may require consent from third parties so it is important to line those up early.

- **Diligence.** Throughout development of the registration statement, the entire IPO team will perform necessary diligence procedures. All parties participating in the registration are liable for any material misstatements or omissions and due diligence serves as the primary defense in any action (other than the company). Diligence often consumes much more time than is anticipated so the sooner materials can be organized, the less of a burden this will be once the IPO process is underway.

- **Offering Process.** There are several steps in the offering process and most companies will think about this in terms of communications and the roadshow but here are a few key items to keep in mind:

- **Testing the Waters.** If a company qualifies as an "emerging growth company", they can partake in testing the water meetings with institutional investors and qualified institutional buyers. Most companies go through at least one round of comments with the SEC to get their story as finalized as much as possible before meeting with investors. Materials used in such meetings must be consistent with the registration statement and will be shared with the SEC. Each investment bank has their own set of procedures including limits on how

many meetings they want the company to participate in. It is helpful to decide early in the process whether such meetings will be necessary and develop an appropriate strategy.

- **Analyst Day.** The analyst day is important and preparation is vital. Unlike the underwriting syndicate, research analysts do not work for the company. They are independent and focused on serving the investor audience who reads their research. These analysts educate the market so it is very important to prepare for analyst day and be able to communicate a clear and concise equity growth story. Analysts will also ask several questions about the management model.

- **Directed Share Program.** Some companies want their underwriters to reserve a certain number of IPO shares for customers, vendors, suppliers, friends and family. The size of this allocation typically does not exceed 5 percent. It is important to consider whether a directed share program is desired and to ensure they are structured in such a way as to avoid running afoul of SEC rules.

Putting it All Together

An IPO process is undoubtedly one of the most stressful events that will take place in the history of any company. With the right people and planning, successful execution is possible. While becoming a public company is no easy feat, the right team and attention to a detailed plan, including the critical path items, will help establish some sense of order in a chaotic process.

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