

Strategies for going public.



Contents

Chapter 1. Should you go public?	1
Introduction	1
The advantages	2
The disadvantages	3
The alternatives	4
The process	4
Chapter 2. Is the time right?	6
Is your company ready?	6
Is the market ready?	8
What if the offering is terminated?	8
Chapter 3. Your team	9
Management	9
Auditors	9
Accounting advisors	9
Attorneys	10
Underwriters	10
Financial printers	10
Others	10
Chapter 4. Prepublic planning	11
Increased formalization	11
Corporate housekeeping	12
Corporate governance	13
Audit requirements	14
A positive image in the market	15
Costs of going public	15
Chapter 5. The underwriters	17
Selecting an underwriter	17
What underwriters look for	19
Selecting a trading market	20
Types of underwriting	20
Pricing the stock	21
Size of the offering	22

Chapter 6. Registration	23
Who does what	23
Due diligence	25
The registration statement	26
The "red herring"	30
Printing	30
SEC review	31
Blue Sky and FINRA clearance	32
Chapter 7. Marketing the offering	33
The marketing process	33
The do's and don'ts of the quiet period	33
The road show	35
Making the best presentation	36
Chapter 8. Closing the deal	37
Signing the underwriting agreement	37
Transfer agents and registrars	37
The lock-up agreement	38
The closing	38
Chapter 9. After you go public	39
Trading and aftermarket support	39
Your relationship with the financial community	39
Compliance with securities laws	40
Chapter 10. Foreign private issuers	44
1933 Act filing and disclosure differences	44
Audit requirements	45
Corporate governance differences	45
After the IPO – 1934 Act filings	46
Appendices	
Appendix A: The U.S. Securities and Exchange Commission	i
Appendix B: Registration exemptions	ii
Appendix C: The Securities Exchanges	iv
Appendix D: A timetable for going public	viii
Appendix E: A sample due diligence checklist	x
Glossary	xii

Chapter 1. Should you go public?

Going public is a long, involved process that represents a significant milestone for any company.

Introduction

You may be thinking of taking your company public and, if so, you undoubtedly have many questions. Deloitte has been advising clients and assisting them in the process of going public for many years. Drawing on that experience, we have prepared this publication to assist you in answering those questions, to acquaint you with the “language” of going public, and to give you a working knowledge of some of the technicalities of the process.

This publication will give you the information that you may need to help you understand the requirements of a successful offering, whom you may need to assist you, what your role will be, certain regulations that must be complied with, and what effect a public offering may have on you and your company. To assist you, we have summarized the contents of each chapter below.

This publication includes a summary description of some of the relevant Securities and Exchange Commission (SEC) rules. These summaries are not complete and you should refer to the rules themselves when preparing to go public, in addition to consulting with your legal counsel.

Should you go public? Public ownership can provide significant benefits to a company and its shareholders, but it has many disadvantages too. This chapter offers you an overview of the process and the pros, cons, and alternatives that should be considered before you decide whether this is the right course for you.

Timing. It is important to evaluate your company’s appeal to investors and the state of the market before you decide to go public. This chapter describes some of the issues the market looks at during an initial public offering, as well as some characteristics of a company considering whether to go public. An appropriate business plan can enable you to move quickly and take advantage of market opportunities.

Your team. Taking your company public requires the talents of a variety of highly specialized professionals. This chapter identifies these professionals and offers a brief overview of their roles in the process.

Prepublic planning. This chapter deals with the steps that you likely need to take to prepare your company for a public offering. It also provides you with an insight into the roles that you can expect your management, attorneys, independent registered public accounting firm (“auditor”), and accounting advisors to play.

The underwriters. One or more lead underwriters are critical to the immediate and long-term success of your public offering. This chapter discusses criteria to use in selecting lead underwriters and, just as importantly, some of the market criteria underwriters use in deciding whether they want to take you public. It also explains the factors they typically consider when pricing your stock.

Registration. Everyone – you, your underwriters, your attorneys, your auditors, and your printers – will be involved in registering your public offering with the SEC. This chapter reviews the importance of “due diligence,” the makeup of the registration statement, and the federal, state, and Financial Industry Regulatory Authority (FINRA) review that your company will need to obtain in order to “go effective.”

Marketing the offering. The actual selling efforts principally occur during the weeks immediately preceding the effective date of your registration statement. This chapter describes that process, the rules governing what you can and cannot do and say during the offering process, and what your involvement in the selling effort should be.

Closing the deal. Once your registration statement is “effective” and the offering is priced, the remaining events in the process of going public occur very quickly.

After you go public. Once the offering is completed, you must look ahead to your responsibilities and duties as the leader of a public company. This chapter explains aftermarket trading, your relationship with the financial community, reporting requirements, and some of the federal securities laws that may affect you.

Foreign private issuers. Many foreign companies consider going public in the U.S. This chapter discusses some of the more important differences between an initial public offering for domestic issuers and foreign issuers.



For many executives of growing companies, going public is the ultimate dream.

Going public can signify, both to the executives and to the outside world, that the company has achieved a special kind of success. Overnight, the company can be transformed from being a closely held entity with a handful of shareholders to a company with a large number of holders of its stock, which can be easily bought or sold through a stock exchange or in the over-the-counter (OTC) market.

On the surface, the transformation from private to public company seems fairly straightforward. A company “goes public” when it sells securities to the general public for the first time. Such a sale requires the company to file a registration statement with the SEC in accordance with the Securities Act of 1933, as amended (“1933 Act”). The 1933 Act requires the registration of securities with the SEC prior to their sale to the public, unless an exemption from registration exists. Additionally, the 1933 Act requires that investors receive financial and other significant information concerning the company. The Securities Exchange Act of 1934, as amended (“1934 Act”), created the SEC and regulates and controls the securities markets and related practices and establishes the ongoing periodic disclosure requirements. While securities may be sold to the general public by other means, the term “going public” refers to those instances where a company, for the first time, uses a 1933 Act registration statement in connection with an offering. The process is also often called the “initial public offering” or IPO.

News about the dramatic wealth created for company founders and members of management that often follow an IPO can be captivating. The prospect of having capital available to finance future growth can be alluring. Yet, careful and deliberate thought is prudent when deciding to go public.

It is difficult to predict what changes will occur in your corporate culture as a result of being a public entity. Opening your company to increased public scrutiny can change the way you do business, and the pressures to maintain growth patterns and meet the expectations of the investment community are typically real and intense. It is advisable to weigh fully the advantages and disadvantages, including those listed in the section below, with a group of trusted advisors. If you decide to proceed, it will be important to plan for the organizational changes that will occur during and after the offering.

The advantages

Going public potentially provides both tangible and intangible benefits, including the following:

Increased capital. When growth can no longer be financed internally, from private equity investors, or through borrowings, an IPO can provide your company with additional funds to meet working capital needs, acquire other businesses, expand research and development efforts, invest in facilities and equipment, or retire existing debt. Publicly traded stock can also be effectively used in mergers and acquisitions.

Improved financial position. As an IPO is usually in the form of an equity-based security, your company will experience an immediate improvement in its balance sheet and debt-to-equity ratio. Significant reliance on debt instruments rather than equity can be a high-risk strategy for growth companies.

Less dilution. If your company is at the stage where it is ready to go public, you may command a higher price for your securities through an IPO than through a private placement or other form of equity financing. This means that you give up less of your company to receive the same amount of funding.

Enhanced ability to raise equity. As your company continues to grow, you may need additional permanent financing in the future. If your stock performs well in the stock market, you may be able to sell additional stock on favorable terms.

Liquidity and valuation. Once your company goes public, a market will be established for your stock. A public market makes it easier to dispose of a portion of your interest for diversification purposes. Subject to SEC regulations (see the discussion of sales restrictions under Rule 144 of the 1933 Act in [Chapter 9](#)), you may sell your stock whenever the need arises. There are important restrictions to keep in mind that place certain limits on the timing and number of shares that can be sold by many parties after the offering.

There are important restrictions to keep in mind that place certain limits on the timing and number of shares that can be sold by many parties after the offering.

Some major shareholders, such as venture capital firms, require liquidity in a company. Venture capital firms generally organize funds with an expected life of less than 10 years. At the end of that period, they typically need to liquidate the fund. By going public, you provide the venture capitalists with the ability to sell their holdings or to distribute publicly tradable stock to their fund participants.

Improved credibility with business partners. The simple fact that you are “public” provides business partners, such as suppliers, distributors, and customers with more information and can be an indication that your company is a business of substance. Prospective suppliers and customers may feel more secure about entering into a relationship with your company. You may also be perceived as a more attractive partner in a joint venture or other similar relationships as a public company.

Better employee morale and productivity. Stock options and other incentive compensation plans enable personnel to participate in the company’s success, without increasing cash compensation. The chance to acquire stock in the company they work for may cause employees to take a longer-term view of the company.

Personal wealth. Not insignificantly, an IPO may enhance your net worth. Even if you do not realize immediate gain by selling a portion of your existing stock in the IPO, you may be able to use publicly traded stock as collateral to secure borrowings of a personal nature. Shares of publicly traded stock are usually more liquid and as such can facilitate personal financial and estate planning.

The disadvantages

There are also some very significant disadvantages of going public that should be weighed against the many advantages:

Disclosure of information. As a publicly held corporation, your company’s operations and financial situation are open to public scrutiny. Information concerning the company, officers, directors, and certain shareholder information not ordinarily disclosed by privately held companies is suddenly available to competitors, customers, employees, and others. Information such as your company’s sales, profits, and the

salaries and perquisites of your officers and directors must be disclosed not only initially, when you go public, but also on a continuing basis thereafter.

Management demands. Top management frequently needs to be available to shareholders, brokers, securities analysts, and the press - all of whom usually want up-to-date information about company progress. Executives (i.e., CEO, CFO) must also be involved in preparing written information about financial results and other company matters that must be reported to the public and the SEC.

Pressure to maintain growth pattern. There can be considerable internal and external pressure to maintain the growth rate you have established. If your sales or earnings deviate from the established trend or from analyst expectations, shareholders may become apprehensive and sell their stock, driving down its price. While a reduced stock price does not have a direct financial effect on a company, it may affect company reputation, employee compensation (through reduced option value, if you have options outstanding) and the viability and value of a subsequent offering (causing more dilution to existing shareholders). In addition, domestic companies will have to begin reporting operating results on a quarterly basis and be subject to additional disclosure obligations. That means that parties can now evaluate your company quarterly, which can intensify the pressure and may shorten your planning and operating horizons significantly. The pressure may tempt you to make short-term decisions that could have a harmful long-term effect on the company.

Less control. The sale of shares to the public will dilute your ownership and may reduce your level of control of the company. In addition, depending on the requirements of your trading market, you are likely to be required to have a Board of Directors consisting of a majority of independent directors. The Board of Directors is responsible for protecting the shareholders’ interests and you will be accountable to them. Additionally, as your ownership is diluted, the possibility for a hostile takeover increases.

Greater legal exposure. As a consequence of selling your company’s shares to the public, there is greater legal exposure for the company and its officers and directors. The offering itself creates exposure under the antifraud rules of the 1933 Act and 1934 Act. All communications, written and oral, relating to the offering can give rise to litigation for securities fraud, if the communications were materially misleading. You will also have to become much more formal in your decision making. Often, private companies operate somewhat informally with respect to director involvement; that can no longer occur with a public company.



Enhanced corporate governance. In response to corporate failures and the loss of investor confidence during the technology bubble, Congress implemented reforms to strengthen corporate governance and restore investor confidence. The Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley Act”) was the most comprehensive reform since the 1933 Act and 1934 Act and holds public companies to a much higher standard of corporate governance than in the past. While this is a welcome change, the cost of being a public company has increased as a result. The extent of the increased cost is partly a function of the quality of your current framework of internal controls over financial reporting. The Sarbanes-Oxley Act also requires an increased amount of involvement for upper-level management of the company in the financial processes of the company. Increased scrutiny over operations as a public company is also mandated by the bookkeeping provisions of the Foreign Corrupt Practices Act, applicable to public companies.

Expense. The cost of going public is substantial, both initially and on an ongoing basis. As for the initial costs, the underwriters’ commission can run as high as ten percent (although typically seven percent) of the total offering proceeds. In addition, you will incur significant out-of-pocket expenses for even a small offering. These initial expenses are discussed at greater length in [Chapter 4](#). There are also significant ongoing expenses associated with periodic public reporting, SEC rule compliance, directors and officers (D&O) liability insurance, independent director fees in the form of cash payments, and option awards and other requirements.

The alternatives

Companies typically make use of a variety of financing options before they even consider going public. Generally speaking, these loan and investment options should be explored and, where appropriate, fully considered before a company decides on a public offering. The most common way to raise additional capital, of course, is to borrow. Loans can be obtained from institutions such as banks, asset-based lenders, and equipment financing companies. The advantages of loans are that they are relatively simple to arrange and will not dilute your ownership. For many companies seeking alternative funding sources, private placements or venture capital may also prove of interest.

Exclusive reliance on debt rather than equity can be a high-risk strategy for growth companies. In incurring debt, you subject your company to potentially significant financial obligations. A downturn in your business or an increase in interest rates could make it difficult to meet your payments. Many companies have faltered in this way.

Companies typically make use of a variety of financing options before they even consider going public.

Another common alternative is to sell your business. The sale of a business will often provide quicker liquidity than an IPO. You will also not be subject to the risk of a decline in the market value of the company after a sale. However, if you sell your business for stock of the acquiring company, you should understand the risks associated with their stock and perform the appropriate level of due diligence on the acquirer. Some companies actually begin the IPO process with the possibility in mind of having that process end in an acquisition rather than an IPO. In both instances, you are marketing your company and many of the early steps in the IPO process can be helpful in an acquisition context. For example, strengthening your internal control over financial reporting framework would assist in the facilitation of your acquisition by a public entity.

When you read about IPOs today, you will see references to reverse mergers and special-purpose acquisition companies (SPACs). A reverse merger is where a private company acquires a public company with only nominal assets; the acquisition results in the private company becoming public. A SPAC involves using the proceeds from the IPO of a company with nominal assets to buy a company, normally within 18 to 36 months of the IPO. Neither will be covered by this publication.

The process

Here, in brief, is the typical general sequence of events involved in taking a company public once an informed decision has been made:

Underwriting. Once you have decided that it would be appropriate for your company to seek a public offering, you invite several investment banking firms, or underwriters, to discuss this possibility. Those who are interested meet with you and your management team to investigate the company’s operations and prospects. The underwriters submit proposals, you select one (or more) firm(s), and the formal process begins (this is covered in greater detail in [Chapter 5](#)).

At this point, you will not have any binding commitments with the underwriters. To help you decide whether to proceed, the underwriters can be expected to provide you with a range of values for the company and what percentage interest in the company that they recommend

be sold. There is usually a series of pricing discussions, and the share price and size of the offering are not finally settled, until just before the stock is ready to be sold.

Registration statement. The 1933 Act requires that a registration statement be filed with the SEC before securities may be offered for sale and that a registration statement be declared “effective” by the SEC before securities are sold. The 1933 Act requires an accurate disclosure of material facts, so that potential investors can make an informed decision about investing in a given security. In addition, the 1933 Act prohibits deceit, misrepresentations, and other fraud in the sale of securities. The SEC does not evaluate the merit or value of the securities it reviews. However, the SEC staff will generally examine registration statements for compliance with the applicable accounting and disclosure requirements.

Preparing the registration statement to comply with SEC requirements is a team effort of management, auditors, and legal and accounting professional advisors. This is usually the most time-consuming step in the process of going public. When the preparation process begins, an all hands meeting is typically held to delegate responsibility for preparing the various sections of the registration statement and to establish a timetable for its completion. When completed, the preliminary registration statement is filed with the SEC.

The registration statement includes the prospectus, which is a brochure or booklet that is used as the selling document. After the preliminary registration statement is filed, the SEC typically reviews it and usually responds within approximately 30 days with comments, questions, and requests for additional information. Those comments can be lengthy. The company modifies the registration statement as necessary, and files an amended registration statement with the SEC. This process can result in several rounds of comments and filings with the SEC. When the SEC is satisfied and the company and underwriters request it, the SEC declares the registration statement effective. In the interval between the initial filing of the registration statement and its effective date (the so-called “waiting period”), the company and the underwriters may distribute copies of a preliminary prospectus. The preliminary prospectus must bear a legend stating that a registration statement related to the offering

has been filed with the SEC, but has not yet become effective and that the securities may not be sold, nor may offers to buy be accepted, before the effective date. Because this legend is printed in red ink, the preliminary prospectus is commonly referred to as the “red herring.” The red herring is typically printed after the company and its advisors conclude that resolution of the remaining comments from the SEC is not likely to require material revisions to the preliminary prospectus and a new circulation to potential investors.

This is the stage, as a practical matter, where the underwriters’ major marketing efforts will move into full swing. By this point, the lead underwriter has usually formed a syndicate of underwriters. As firms join the syndicate, their salespeople begin distributing the red herring to clients and orally soliciting orders; these orders are considered as indications of interest only and may be canceled by the customers after receipt of the final prospectus. The lead underwriter builds a “book” of these orders, which will help in the pricing of the offering and ensure strong demand when selling is allowed. Generally, the lead underwriter wants the book to contain orders for more shares than it intends to sell, so that there will be demand for shares even after the offering. Also, the road show generally occurs during this period; this is a tour that enables the company’s executives to meet the underwriters’ salespeople and prospective investors. It, too, is designed to build momentum for the offering and is scheduled to end just before pricing occurs.

Immediately before the registration statement becomes effective, the company files the final prospectus, again without the pricing information, to reflect the resolution of all of the SEC’s comments. Then, within a matter of days (and often on the same day), the registration statement is declared effective, the final negotiations with the lead underwriter on share number and pricing are completed, and the offering commences. Immediately thereafter, an amended prospectus is filed to reflect the pricing information. The final prospectuses are then distributed to customers.

Closing and sale. As with most financing transactions, a closing is held after the registration is effective and the offering commences. The securities are delivered to the underwriters for distribution to or on behalf of their customers, and the proceeds, net of underwriting commissions, from the sale of stock are paid to the issuer. The closing usually takes place within a week after the pricing, giving the underwriters time to receive payment for the securities from most of their customers in response to the confirmations of sale which have been sent.

Preparing the registration statement to comply with SEC requirements is a team effort of management, auditors, and legal and accounting professional advisors.

Chapter 2. Is the time right?

Is your company ready?

Honestly assessing the interest that your company is likely to generate in the public market is the first step toward a successful IPO. While there is no universal law to determine market interest, past experience indicates that market appeal can be predicted by certain guidelines that are indicative of the company's maturity and potential for future earnings.

A focused business plan is an important part of your IPO. It contains future operating projections, such as budgets and forecasts, that are not contained in the registration statement, but that will likely be essential to you as you sell your story to the lead underwriter. Your management team will need to clearly articulate a compelling strategy to the underwriters and potential investors to help you realize a valuation reflective of your company's potential.

Any prospective investor in your company will look at a number of factors in making its decision to buy your stock. As the representatives of the purchasers, the underwriters often need assurance on these factors in order to sell your stock with confidence. They need to be enthusiastic about your company's potential and about the industry; they need to be confident that there are no significant negative factors (e.g., susceptibility to technological change, increased competition, and recession-induced problems) with which the company cannot deal, and they must have confidence in the people running the company.

Below are some of these factors and questions that are typically asked with respect to them:

Management quality. This is a very important factor for investors. Investors will typically entrust their money only to a team with strong leadership. Questions include: Do the top managers have the necessary experience? Do they work together as a team? Are they of high integrity? Do they inspire confidence among the company's employees? Do they have long-term potential? Are they effective in developing working relationships with customers, suppliers, bankers, auditors, etc.? Is there stability in the leadership team? The departure of a key executive just before or after the IPO will potentially affect the company's market competitiveness and raise concerns with potential investors.

The underwriters (and investors) will also look at the composition and qualifications of members of the Board of Directors. If the board needs to be upgraded as a part of the IPO process, your advisors can assist you in doing so as a part of the preplanning process. See [Chapter 4](#).



Employees. A strong employee base is important to the success of most companies. Questions include: What is your human resources strategy? How do you attract and retain top talent? What are your compensation, stock option, and employee benefit plans? How do they compare to others in your industry? Is there an adequate labor supply to support your growth plans? If some of your company's employees are represented by labor unions, how are your relations with the unions and what is the status of your labor contracts? Are you dependent on only a few key employees and, if so, how are you protecting yourself from the risk of their potential departures?

Product quality and industry potential. The quality and future of your products in the context of your industry is key. Questions include: At what segment of the market are you aiming? What is the growth potential? Who are your competitors? How long a life do your products have? Will you have to diversify or develop new products to continue growing? Does your company have command of its technology? What products are in research and development? What is your product roadmap? Are you in a growth industry? How permanent is that industry?

Production or service capability. Your ability to execute operationally on your business plan is also key. Questions include: Are your production facilities or product-sourcing arrangements adequate to meet the demands of growth? How do your production capabilities compare with others in your industry? Are they adequate to meet the quality requirements of your market? How efficient is your supply chain? What risks are inherent in your supply chain? Are your information systems adequate to support inventory forecasting? What are your contingency plans if there is an interruption in the supply of key raw materials, shipping, or other key aspects of product production?

Financial position. Your current financial position is important in assessing both how much money will need to be raised and how effective your financial management is. Questions include: How well you are managing your assets? How are you financing your working capital needs? Are you providing any financial support to your customers? What financial contingencies exist? How leveraged are you and what is your effective cost of capital? Do you have audited financial statements?

Earnings history and potential. Reported earnings and potential future earnings are often considered as important for public companies as cash flow is for private companies. Questions include: What has your earnings history been? What is your growth potential? Is there a strong upward trend that is likely to continue? How do you compare (in earnings and margins) with other companies in your industry? Do you have detailed historical and future information about your operations, including sales and gross margin analyses by product or product line, sales channel mix, geographic sales breakdown, and headcount trend reports?

Company reputation. Investors will consider your reputation in making investment decisions. Questions include: How do suppliers, customers, experts, and others in your industry assess your performance? How does the public perceive your company? What kind of relationship do you have with your customers and your suppliers?

A company that offers the investment community a high-risk/high-reward opportunity likely will be held to evaluative criteria that differ from those applied to a company that is perceived to be a long-term solid performer. Taking this into account, most companies fall into four general classifications: early-stage, high-growth, long-term solid performers, and spin-offs.

Early-stage companies

Some companies' potential so captivates the public's focus that they can attract funds. These companies receive considerable attention when they go public even though they may have yet to produce significant revenues. Some of these companies are bolstered by the strengths of a promising industry, such as biotechnology, while others rely on the past performances of similar enterprises that have achieved significant growth. More typically, however, early-stage companies have reached the point in their development where most of the technological, manufacturing, and marketing risks have been substantially reduced, and their stock can command a higher price than venture capitalists are willing to offer. The market appeal for this type of company is heavily influenced by three factors:

Market opportunity. An industry that can support significant growth.

Potential industry leadership. An unproven company needs a product that indicates it is on the leading edge in its field.

An experienced management team. Management personnel demonstrate the capability to deal with anticipated growth and to maintain the company's leadership position.

High-growth companies

High-growth companies also offer the potential for significant future growth, and they have typically matured beyond the "start-up phase" to attain a certain level of revenues and profitability. The market most readily accepts companies of this type that have achieved the following:

Sales. With some exceptions, annual sales of at least \$50-\$75 million suggest an established company.

Proven profitability. Net income of \$1 million or more in the most recent fiscal year is usually sought, although just a few quarters of profitability may be sufficient in certain markets.

A growth track record. The investment community generally looks for an annual growth rate of 25% or more with the ability to maintain that rate in the next few years.

An experienced management team. Institutional investors in particular want evidence that the company does not rely on the talents of a single entrepreneur. Normally, the founder is surrounded by experienced executives with responsibilities for key management areas.

Long-term solid performers

These midsize companies often have a long and continuous record of strong sales and earnings. They may not be nationally known, but they offer the public a long-term investment at a reasonable price-earnings ratio (calculated by dividing the price per share of common stock by earnings per share). Despite their profitable history, established companies may go public for several reasons, such as to fund acquisitions or provide liquidity to their owners. In many cases, they have sales of several hundred million dollars; a large, stable or growing market; and a profit history equal to or better than the industry average.

Spin-offs

A number of large companies that operate in several segments have spun-off divisions or segments as a way of realizing shareholder value.

Demands of being a public company

In addition to the potential market appeal of your company, you must evaluate the capability of your management team and the strength of your internal systems and processes (particularly your financial systems and internal controls) to meet the demands of being a public company. You must be able to meet the periodic disclosure requirements of the 1934 Act and communicate with the financial community about your operations and prospects. Additionally, you will need to assess your Board of Directors' qualifications relative to the requirements of the Sarbanes-Oxley Act and the National Association of Securities Dealers Automated Quotations (NASDAQ) and the New York Stock Exchange (NYSE) listing requirements.

Is the market ready?

The market can be influenced by a variety of factors, including economic forecasts, political events, international trends, interest rates, and inflation. A company that might easily attract public funds in a bull market could run into considerable resistance in a bear market. When the market becomes depressed, declines in value are generally greater for newer, less-established issues and companies in "riskier" industries.

The market for IPOs can also completely dry up as it did in the summer of 1998 following adverse economic events in Asia, in 2001 and 2002, following the corporate governance and accounting scandals and the dotcom bubble and in 2008, following the financial crisis; however, if an offering is fortunate enough to catch a rising market, an IPO may produce a windfall of capital. You should rely on thorough preparation, the expertise of your IPO team, and patience to guide your company through this decision. At the same time, consideration should be given to alternative financing, such as that provided by mezzanine venture capital investors to protect the company in the event of an unanticipated "closing of the IPO window."

What if the offering is terminated?

The market opportunity to do an IPO can be quite short and on occasion, due to a variety of reasons, companies terminate their registration statement before the securities are sold. Historically, this could cause problems for future financings, since the registration statement was a public document. To address this issue and allow a quick conversion to a private offering, in 2001, the SEC adopted Rule 155, which allows companies that have filed a registration statement and then withdrawn it to implement a private placement of securities within 30 days after the withdrawal of the registration statement if certain disclosures are made to the private placement investors. In addition, terminating a public offering before it is finished does not impact the ability to sell the company. In both cases, much of the work done for the public offering can be utilized in either the private placement or the sale transaction.

The market can be influenced by a variety of factors: economic forecasts, political events, international trends, interest rates, and inflation.

Chapter 3. Your team

Taking your company public requires the talents of a variety of highly specialized professionals.

Underwriters, auditors, legal and accounting advisors, and financial printers. There may also be a role for financial public relations professionals, and as you near the closing, you will need to have a transfer agent and registrar. This array of professional services providers and the time demands made on company management will be costly; however, these costs should be viewed as simply one price of going public. The success of the IPO and the future prosperity of the company may depend, in part, upon the talents of this team, so you should resolve to engage the most qualified people available.

Management

Throughout the IPO, management will serve as the tangible representatives of the company. The importance of its impression on the investment community should not be underestimated. Investors typically place enormous weight on their perceptions of management's abilities; thus, management's qualifications, ethics, and experience will likely be highly scrutinized. One way to address this is to make a concerted effort to retain executives who are experienced in building a company and taking it public and who do not have ethical issues associated with them. Executives with a successful history of corporate growth can substantially help to alleviate the fears of investors.

The organizational structure is usually headed by at least a Chief Executive Officer (CEO), and a Chief Financial Officer (CFO). Additional executives that may be useful depending on the industry are a Chief Information Officer and a Chief Technology Officer, and, depending on the size of the company, a Chief Operations Officer. Most public companies also have a general counsel.

Management is an essential participant in both the preparation for, and the marketing of, the offering. During the pre-filing period, management's intimate knowledge of the company is important in making certain the story of the company told in the registration statement is accurate and complete. After the filing, the centerpiece of the marketing effort is the road show. This is a tour by top management, with the lead underwriter, to a dozen or more cities to allow management to meet with underwriters, analysts, and potential investors, present strategic, financial, and operational reports and answer questions. See [Chapter 7](#).

Management is also the link between the IPO team and the company's Board of directors. The board should be fully supportive of the IPO and will have to sign the registration statement and take on securities law exposure as a part of the process.

Auditors

An important part of the prepublic planning effort is to assess

your company's financial house to consider if it will satisfy strict SEC and underwriter demands. One step is to consider your external auditor relationship. Your external auditor should be a qualified public accounting firm that has significant SEC experience and is registered with the Public Company Accounting Oversight Board (PCAOB). The issuer's annual financial statements must be audited by a public accounting firm that is registered with the PCAOB. Because of their industry specialization and extensive SEC experience, many companies choose to engage the services of one of the prestigious international professional service firms.

In addition to completing the audit of your financial statements and assisting you in the preparation of any interim financial statements for the registration statement, your auditors will also render significant assistance in the registration process. They will read any other financial data to be included within the registration statement and, in doing so, may be able to highlight concerns the SEC may have related to the registration statement and to help you address these in the filing. They will also assist in the responses to the SEC's accounting-related comments. All of this will reduce the possibility of subsequent delays and revisions. Clearly, your auditor's role is a large one and one that would be facilitated by establishing a good working relationship early in your company's development. In this way, they can serve you better through their intimate knowledge of your company's particular situation.

The auditor will furnish comfort letters (see [Chapter 6](#)) to the underwriters, which assist the underwriters in performing their investigation of certain financial and accounting data that is included in the registration statement.

Accounting advisors

In your prepublic stage, your accounting (and legal) advisors can assist you by making introductions to underwriters to ascertain their interest in your IPO, compiling data so that you may evaluate the compensation proposed by the underwriters, and providing consultation and advice in your negotiations with the lead underwriter concerning financial matters to be included in a letter of intent (if there is one) and in the final underwriting agreement.

In addition to the accounting, auditing, and SEC experience that you will need to call upon, many growing companies need advice on other key issues associated with growth, such as the size and additional competencies necessary to staff an accounting and finance function in a public company and general business planning advice. These are important areas that accounting advisors should have the expertise to help you address.



Attorneys

Going public is a highly technical legal process and you will work closely with your attorneys as they assist in your offering. SEC legal work is very complex and highly specialized, and there are serious penalties, as well as the risk of shareholder lawsuits, for all of the parties involved in the issuance of a registration statement that omits critical facts or contains misleading or false information. It is extremely important that you have legal counsel with prior SEC experience and knowledge of the intricacies of working with the SEC.

Your counsel assists in the process of preparing the registration statement and responding to the SEC's comments. Experienced SEC counsel (like experienced accounting advisors) can also speed the process significantly, which can reduce costs and allow a more effective marketing process. They also advise you on all the preplanning process, including what communications are allowed throughout the process, and providing critical legal opinions during the process. As a part of the registration statement, they opine on the legality of the stock being issued or sold in the IPO and, at the closing, they issue a legal opinion on a variety of subjects to assist the underwriters in their due diligence process.

Underwriters

A lead underwriter, or investment banker, leads the marketing of the IPOs. These professionals are selective in their acceptance of clients and likely will conduct in-depth research into your company's management, products or services, finances, and business plan before accepting your company as a client. A key task for the lead underwriter, after accepting a client, is to determine the value of the company according to industry and market analysis. The lead underwriter likely will create a syndicate of as many as 30 underwriters to market and sell the securities. If the stock falls below the IPO price within the first few weeks of its debut, your lead underwriter may seek to stabilize the stock's aftermarket performance. (The role of your lead underwriter is extensive and is discussed in greater depth in [Chapter 5](#).) In many cases, a successful IPO signals the beginning of a long-term relationship between your company and the lead underwriter. Remember that even though you are the client of the lead underwriter, there are some inherent conflicts of interests between you and the lead underwriter; most importantly, the lead underwriter also has preexisting relationships with most institutional customers who will be buying your stock (as well as the stocks of other companies that are being offered on an ongoing basis through the underwriters).

Financial printers

The SEC maintains strict guidelines on the format of registration statements and prospectuses it will accept. These documents

must not only be printed to technical standards, but must also be accompanied by an electronic submission to the SEC's Electronic Data Gathering Analysis and Retrieval (EDGAR) system. As financial printers, these firms stay up-to-date on SEC requirements and are accustomed to the time constraints and confidentiality issues involved in their work. Typically, these printers also maintain facilities with conference rooms and other amenities that accommodate the unique conditions that often surround the printing and filing of SEC documents. Additionally, some attorneys now offer EDGAR services.

Others

Public relations is often neglected, yet can be worthwhile to consider in connection with an IPO. An effective campaign can serve as a means of increasing the public profile of your company. While you can maintain your prior level of business communications (such as for product announcements), any efforts targeted at the financial community must be suspended once you commence the IPO registration process and enter the "quiet period." After the offering, the role of financial public relations or investor relations is critical. These efforts can work to retain existing shareholders while attracting new investors, thereby maintaining or raising the stock price; often, when the marketing effort stops, your public visibility is reduced. Effective financial public relations takes time, and you should cultivate a relationship with a reputable firm as early on as possible. Your underwriters, attorney, or other accounting advisors can usually recommend an experienced firm.

Transfer agents and registrars are also important in the technical side of share issuances and transfers. They specialize in maintaining shareholder records. Transfer agents are required by both the NYSE and NASDAQ and, while optional, are highly recommended for any OTC issue not listed a national securities exchange. Besides maintaining shareholder records, transfer agents assist in stock transactions, meet the requirements of the Internal Revenue Service, and coordinate shareholder correspondence and dividend payments. Registrars, who are usually part of the same firm, keep track of all issued stock and safeguard against over-issues. Your attorneys or other accounting advisors can usually recommend a reputable firm. The transfer agents and registrars are not part of the preparation process, but are added sufficiently in advance of pricing so that the actual sale of the securities can occur smoothly.

A key task for the lead underwriter, after accepting a client, is to determine the value of the company according to industry and market analysis.

Chapter 4. Prepublic planning

Once you decide that you want to take your company public, you are embarking on a journey.

Going public is not something you just do one day or one month. It takes long-term planning and many months, or even a year or more, to effect. This prepublic planning is necessary both to prepare to sell stock and to demonstrate to the lead underwriter that you are ready to be a public company.

This chapter discusses six issues we recommend that executives begin to address before approaching investment bankers.

It is important to address issues, such as the provisions of your stock option plan, before the offering commences.

Increased formalization

Running a private company for a handful of investors is vastly different from running a public company for a large number of shareholders. While even as a private company, you have had a fiduciary responsibility to all of your shareholders, as a public company, your actions will be much more visible, which will require you to be more formal in managing the business and complying with all of the requirements imposed by federal securities laws. You should be aware of the consequences well before you transform your business into a public company. (Some of the most significant consequences are discussed in [Chapter 9](#).)

We recommend you and your management team be psychologically ready and appropriately staffed to accept these added responsibilities. To prepare yourself, begin to operate as if your company were public well before you formally seek to go public. This means doing the following:

Maintain adequate records and internal controls. Learn to generate reliable and meaningful monthly financial statements promptly after month-end so that, when quarterly reporting is required, the mechanisms for producing these reports are already in place. Your accounting and financial departments should expect to have monthly and quarterly closes that are as accurate as a year-end close. This is crucial on a prospective basis when filing quarterly reports on Form 10-Q and responding to analysts' inquiries. In addition, you may be asked to present historical quarterly information for inclusion in your prospectus. You should evaluate the personnel in the accounting and financial departments to make sure that the quantity and quality of personnel are currently employed to complete these additional responsibilities.

Remember, in accordance with the rules under the Sarbanes-Oxley Act, once the company is public,

management will need to certify the financial statement's accuracy and, as such, management should be involved in the financial statement closing process on a quarterly basis.

Monthly reporting packages typically include, at a minimum, information that will permit analysis of sales volume and pricing trends by product or product line; sales by major customers, sales channels, and geographic regions; and headcount trends. In addition, major balance sheet items (e.g., accounts receivable and inventory) should be supported with appropriate analysis. In receiving timely financial information, managers can discipline themselves to analyze operations and results more frequently and accustom themselves to the pressure of quarterly performance evaluations. The investment community generally reacts negatively to financial "surprises."

Management should also begin designing, implementing, and documenting its internal control processes. Once the company is public, management will be obligated to certify as to the effectiveness of the company's internal controls over financial reporting process.

Bring your stock ownership records up to date. One of the more time consuming aspects of preparing the registration statement can be determining the ownership, both direct and beneficial, of your stock and agreeing on the details of stock information for the registration statement and related financial statements. This includes determining if all the proper legalities were observed in the issuance of the stock, from both a corporate and a securities law perspective, and identifying any registration rights that shareholders may have. It also means addressing any issues related to employee stock option and other stock-based compensation plans, including knowing about all unexercised options that may have been granted and determining whether these options are vested. If not addressed sufficiently in advance, these matters could lead to expensive delays in the registration process. The SEC often raise valuation issues with respect to recent stock issuances or with the pricing of recent option grants, if pricing is to be significantly below the likely initial public offering price. You should talk with your legal and accounting advisors carefully about these matters before you start the IPO process.

Upgrade the directors and expand their role in overseeing policies. Before your company goes public, you should take a critical look at your board of directors. The board of directors will assume more responsibilities as a result of the company going public, and the members' credentials should appropriately suit their responsibilities. In addition, prospective investors in an IPO will review the board members' credentials to see if they have confidence



in the board members' ability to oversee a public company. If your board of directors consists of friends and relatives who do not have the necessary credentials, you should consider changing the composition of the board of directors and seek out independent industry experts or executives of noncompeting companies with related products or services. Organizations such as the National Association of Corporate Directors can be very helpful in providing guidance in this regard. Additionally, the [American Institute of Certified Public Accountants \(AICPA\)](#) has a system on their [Website](#) where you can search for qualified candidates to serve on your board of directors and the audit committee of your board.

You should also engage the directors in reviewing and approving company policies and strategies and in reviewing operating results and trends. The board needs to establish an audit committee to oversee the appointment of an auditor. Additionally, the audit committee should be involved in the oversight of the scope and results of the audits of the financial statements and effectiveness of internal controls over financial reporting. See further discussion of the board of directors and the audit committee under Corporate Governance later in this [Chapter 4](#).

Corporate housekeeping

Once you make the decision to go public, you will likely need to do a substantial amount of preliminary work not directly related to the preparation of the registration statement. Attorneys refer to this as corporate housekeeping.

Determine whether the company is legally positioned for an offering. Counsel's role in the offering will begin with advising you as to whether you should even undertake an IPO. Consult with counsel to determine whether any pending litigation could impact the company's ability to go public. In addition, you may have arrangements, such as royalty agreements, that need to be revised before you are marketable as a public company. You, together with counsel, should also examine whether you are in compliance generally, including with the FCPA, export controls and environmental regulations.

Conduct business through a clear organizational structure. A company going public should have an organizational structure suitable for public investment. Many closely held businesses are conducted by a number of corporations under common ownership or by combinations of business entities. They can be operated as limited liability companies or as Subchapter S corporations; both provide for pass-through tax treatment that can be more tax efficient. The company should carefully consider how its current

business structure may affect the increased financial reporting requirements of a public entity. Considerable work may be required to reorganize the various entities by mergers, liquidations, and for additional capital contributions.

Simplify the capital structure. Some companies planning to go public have to make significant changes with their organizational or capital structure. Even when the business has been operated as a single corporation, the capital structure may need revision. You may need to simplify a complex capital structure by redeeming dilutive securities, such as stock warrants and preferred stock, or converting them to common stock. The number of shares currently authorized and the number you have outstanding will affect your offering. You may need to amend your corporate charter to authorize the issuance of more shares to be sold in the IPO. If you currently have only a minimal number of shares authorized and outstanding, you may want to split the stock (or in the case of a very large number of shares outstanding, use a reverse stock split) to bring the number of shares and the price of the stock to an acceptable level for the offering. While planning for these actions should occur early in the process, often they are completed simultaneously with the completion of the IPO.

Review all related-party transactions and material contracts. Generally speaking, you will need to depersonalize your business before taking it public. The SEC requires full disclosure of significant related-party transactions. You must disclose the names of highly compensated individuals, the amount paid to them, and any special arrangements made with them. These arrangements should be considered in light of how they will appear to the public. Shareholders' agreements providing for rights of first refusal may have to be canceled; loans made by the company to members of management or by insiders to the company may have to be repaid; the fairness of the terms of contracts (such as leases) between the company and insiders should be adequately documented and, if necessary, altered; and employment contracts, stock option plans, and stock purchase plans may have to be entered into, revised, or canceled. Additionally, the Sarbanes-Oxley Act generally made it unlawful for a company to extend or maintain credit, or arrange for the extension of credit in the form of a personal loan to or for any director or executive officer of the company.

A company going public should have an organizational structure suitable for public investment.

You should review all your material leases and contracts, updating or revising them to reflect their current terms or to provide more flexibility. You should review your balance sheet and off-balance sheet assets, like intellectual property) to determine whether you can verify the legal ownership and existence of all your assets. You should make certain you have all the documentation regarding your outstanding loans and notes and that there are no provisions in them that may cause you to be in default as a result of the actions you intend to take in going public.

Anticipate major company initiatives. During the registration process, you should consider the consequences of undertaking any significant company initiative. A major initiative in the middle of your registration process may necessitate revisions of your prospectus, another filing with the SEC and a new circulation of the preliminary prospectus. To avoid any possible delay in registration, the impact on the offering of any major initiative should be considered. It may be beneficial to complete (or abandon) major acquisitions, and to finalize the establishment of any new management compensation program, new royalty and lease agreements, and changes in key personnel and directors before you begin the registration process.

Orderly finances. The SEC requires that your company's finances be sufficiently detailed and your financial statements audited in preparation for your IPO. You should engage an auditor as early as possible to identify any unforeseen financial obstacles that may have detrimental consequences if uncovered later in the IPO process.

Corporate governance

Board of directors and audit committee

In the United States, every corporation has a board of directors; for private companies that is typically comprised of company executives, shareholders, and, in some cases, independent members. The board of directors of a public company typically is, and is required to be within 12 months of the IPO, if its stock is traded on a national trading system or stock exchange, comprised of a majority of independent directors, including one designated as a financial expert who will also be a member of the audit committee.

Each public company is also required by the SEC to have an audit committee in place. The audit committee has responsibilities, which include that there be procedures in place to handle complaints regarding accounting, internal controls, or auditing matters. The Sarbanes-Oxley Act requires the audit committee to be directly responsible for the appointment, compensation, and oversight of the auditor, including the resolution of any disagreements

between management and the auditor. Each member of the audit committee must be independent. However, in connection with an IPO, a limited exemption exists regarding independence. The audit committee is required by the SEC to have at least one fully independent member at the time of the IPO completion, a majority of independent members within 90 days, and a fully independent audit committee within one year. If the audit committee does not have a financial expert, the reason would need to be disclosed within the company's annual filing with the SEC.

The SEC also sets forth disclosure rules on corporate governance matters. These include the number of board and committee meetings and attendance at those meetings, the presence of nominating and compensation committees of the board (and if those do not exist, why the board determined not to have those committees), whether the company has a code of ethics (and if not, why not), and whether the board has a process to allow shareholders to communicate directly with the board (and, again, if there is no such process, why not). Effective February 28, 2010, additional disclosure will be required as to whether the board has separated the roles of CEO and chairman (or has a lead independent director) and, if not, why not, and what the board's role is in risk oversight for the company. There are accommodations for smaller reporting companies.

While the SEC's approach is generally disclosure oriented rather than creating substantive corporate governance requirements, the NYSE and NASDAQ do have substantive rules on corporate governance in addition to the SEC rules. The NYSE's rules include provisions relating to compensation and nominating or corporate governance committees, as well as additional requirements for audit committees, a requirement for codes of business conduct and ethics and corporate governance guidelines, a requirement that companies have an internal audit function, and a requirement for executive certifications related to corporate governance. The NASDAQ's rules include additional provisions for the Board of directors and audit committees and for independent director oversight of executive compensation and the director nomination process, and requirements for a code of conduct. These rules can be important in your determination of what market you want your stock to trade on after the IPO. Both also have rules on other corporate activities, such as requiring shareholder approval of certain material transactions. You should consult with counsel on these requirements and their effect on your company prior to attempting to file your IPO.

Charter and by-law provisions

This pre-filing period is also the opportunity to consider what type of corporate governance provisions are wanted in the

articles of incorporation and by-laws as a new public company. Private companies often have provisions that are appropriate for a company with a limited group of owners (such as preemptive rights to purchase equity or rights of first refusal) that are not appropriate for a public company. These should be removed. Others, such as special voting provisions, need to be considered to determine if you want them to remain.

As a public company, you will also be more vulnerable to attempts at changes in control in situations where the board does not believe that it would be in the interests of the shareholders as a whole. Certain provisions can be added to the articles of incorporation and by-laws that can assist the board in representing the interests of the shareholders. Among the provisions to be considered are whether the company will have two classes of common stock with differing voting rights, whether it will “classify” its board of directors into three classes, with each class having three-year terms, and whether there will be any supermajority voting requirements for amendments of the articles of incorporation or by-laws. There are a series of such provisions and you should consult with counsel about their costs and benefits. Since these can impact valuation, you should also work with the lead underwriter as you consider whether you want to include some of these provisions.

Audit requirements

General

Under SEC rules, domestic companies (other than smaller reporting companies) must include three years of audited annual financial statements in an initial registration statement. Smaller reporting companies must include two years. In addition, unaudited interim financial statements may be required. Auditors must perform certain review procedures on interim financial statements.

If your company has recently grown through significant merger and acquisition activity, or an acquisition is probable, financial statements of the businesses that were acquired or may be acquired may also need to be presented and audited. If your company has a significant investment accounted for under the equity method of accounting a full set of financial statements of the investee may be required. Separate financial statements of financial guarantors may also be required. The SEC requirements are complex, so you should check with your counsel or your auditor early in the process to be sure you understand the specific requirements. In some cases, the underwriters may require you to have more periods of information audited than are strictly required by the SEC to give potential buyers more confidence. You should reach agreement with your underwriters on their recommendations to go beyond SEC requirements early in the process.

The SEC requirements are complex, so you should check with your counsel or your auditor early in the process to be sure you understand the specific requirements.

See [Chapter 6](#) for additional information about the financial statements required in a registration statement.

Because of these extensive audit requirements, many companies establish a relationship with an auditor very early in their development and have annual audits performed, even if the shareholders or debt holders do not require them. Then, once the decision is made to go public, audited financial statements will be available.

Having a two- or three-year audit performed in the process of going public can be time consuming. Therefore consider having annual audits performed currently, in the years leading up to your initial public offering. Additionally, you should keep adequate records to be able to determine quarterly results, if necessary. It may be more difficult to have a two- or three-year audit performed as part of the process of going public for several reasons:

It may not be feasible. If you have significant inventories, your auditors generally need to observe and test your annual physical inventory counts in order to issue a “clean” opinion for each of the years under audit. This cannot be done after the fact except possibly by a costly audit of a “roll back” of a current physical inventory.

You may be surprised at the audit results. Income results and trends may not be as you had expected and may lead you or the underwriters to cancel or delay the IPO; by this time, you will have incurred substantial costs.

Further delays could result. A two- or three-year audit is time consuming and could delay the registration process by several months. A few months’ delay could mean missing the “window” when it would be most advantageous for you to go public.

Improved financial reporting. The auditors may also generate useful suggestions to organize your accounting records, internal controls, and processes. Prior to the IPO process, it is recommended that the company document its internal controls and processes. Section 404 of the Sarbanes-Oxley Act (“Section 404”) requires that

management certify as to the effectiveness of the company's internal controls over financial reporting process. In addition, subsequent to registration, the company's auditors may be required to opine on the effectiveness of the company's internal control over financial reporting (see [Chapter 9](#) for additional information).

A positive image in the market

Just as your company goes to great lengths to create a favorable public image for its customers and products, it should try, to the extent legally permissible, to create a favorable image for the people who will buy your stock or can influence that buying decision. These people include financial analysts, stockbrokers, the business press, publishers of newsletters, and specialty publications that follow your industry from a financial standpoint. Here are some ways you can get started developing a positive image:

Begin a financial public relations program. Name recognition can be a very important factor in pricing your stock, but it cannot be developed overnight. As discussed in [Chapter 7](#), the type of publicity you can seek out is limited once you have made the decision to go public. Consequently, it is important that you begin trying to raise your public image with the appropriate people at least a year before you plan to go public. In these conversations, do not mention any possible offering. Because effective financial public relations require a special skill, you might consider engaging a financial public relations firm that is experienced in working with the business press and securities analysts. Many entrepreneurial companies publicize one or two key individuals, such as the founder or a chief scientist or technologist. Financial analysts and the business press, however, like to probe more deeply into the company. You should certainly continue to focus attention on your key individuals, but demonstrating your depth of management and operating talent can be just as important.

Make presentations at conference and trade shows.

Trade associations, investment banking firms, venture capital conferences, and business media organizations frequently have conferences at which companies can present themselves to the press and analysts. If these exist in your industry, arrange for a presentation of your company. In addition, analysts frequently attend major trade shows and technical conferences to keep abreast of products in their fields. The key analysts will likely attend shows where you exhibit. Make a special effort to demonstrate your product and introduce your key managers and engineers, but limit your discussions to nonfinancial information or publicly disclosed financial results as applicable to your ownership status at that time (for reasons further discussed in [Chapter 7](#)).

Costs of going public

The costs associated with going public are significant, but there are opportunities to control these costs. The main costs come under the following categories:

Underwriters' expense

The underwriters' discount, or commission, is typically the largest single cost of going public. It is negotiated between you and the lead underwriter. Factors that affect the discount are the size of the offering, the type of underwriting (see [Chapter 5](#)), the going rate for offerings of similar size and complexity, and the efforts perceived to be required to sell your stock. In smaller offerings, underwriters may seek other compensation, such as reimbursement for some of their expenses, warrants to purchase stock, or the issuance of stock to them prior to the offering at a price below the anticipated price to the public. All of the compensation paid to the underwriters (or related persons) is subject to review by FINRA to ensure that it is not "unfair or unreasonable."

Out-of-pocket costs

Apart from the underwriters' discount, you will incur significant out-of-pocket costs, primarily for professional advisor fees (accounting and legal), audit fees, and printing. The costs vary a great deal, as each offering is unique. If unusual problems or circumstances develop, such as an unforeseen accounting surprise, the costs could increase substantially. You can find the out-of-pocket expenses for other IPOs by looking at the SEC's website for registration statements of other issuers doing IPOs; Item 13 in Part II of the registration statement summarizes the expenses of the issuer in the offering.

Legal expense. Legal fees are incurred for the preparation of the registration statement, negotiation of the underwriting agreement, housekeeping, due diligence, and other matters that arise during the IPO process. If the housekeeping is extensive, requiring a complex reorganization or the negotiation of significant contracts, the legal fees will be higher.

The fees will also increase if there is a large number of selling shareholders because of the legal and administrative work for each seller. In secondary or partial secondary offerings, some of the legal and other fees may be borne by the selling shareholders. Those shareholders and the company determine the allocation of expenses; however, often the company bears many of the expenses (other than the underwriters' discount attributable to the selling shareholders' shares).

In most cases, you also pay a special fee to the underwriters' counsel for work in connection with Blue Sky filings, when required and FINRA clearance (explained in [Chapter 6](#)).

Audit fees. Audit fees are incurred for the audit of the financial statements, as well as the auditor's participation in the process associated with the preparation of the registration statement and the comfort letters for the underwriters (explained in [Chapter 6](#)). The fees will increase significantly if separate financial statement audits of businesses acquired or to be acquired, equity method investees, or financial guarantors are required. Also, if interim financial statements are required, the audit fees will be higher, as the auditors will have to review them, particularly in connection with the comfort letters requested by the underwriters.

Printing costs. You will need to have the registration statement and prospectus and all amendments, and the stock certificates printed. Printing costs vary, depending on the length of the prospectus, whether color printing is used, and the extent of the revisions required. Significant savings may be realized by preparing pre-filing drafts internally.

D&O liability insurance. The cost of D&O liability insurance may be several hundred thousand dollars for a company going public, depending upon the amount of coverage and market conditions. The coverage relates to liability arising under the 1933 and 1934 Acts. Such liabilities can result from shareholder lawsuits relating to disclosure or omission of disclosure and errors in the companies' SEC filings.

Miscellaneous expenses. Other out-of-pocket costs include the SEC filing fee, the NASDAQ or NYSE filing fee, any Blue Sky filing fees, and registrar and transfer agent fees. Each of these can range from several hundred to thousands of dollars. If the underwriters, company counsel, and the printer are in different cities, substantial travel and telephone charges are likely to be incurred. You will also need to include the cost of the road show and public relations expenses in your budget. In addition to these identifiable costs, significant executive and administrative time will be spent as officials assist in putting the offering together.

From a financial statement perspective, many of the costs associated with a successful offering can be offset against the proceeds from the offering on your balance sheet rather than charged directly to the income statement. For instance, specific incremental costs incurred prior to the effective date of an offering may be deferred and charged against the gross proceeds of the offering. Management

salaries or other general and administrative expenses, may not be allocated as costs of the offering and, therefore, cannot be charged against the proceeds of the offering.

Deferred costs of an aborted offering may not be deferred and charged against proceeds of a subsequent offering and, therefore, must be written off. A short postponement (up to 90 days) does not constitute an aborted offering. Therefore, should you decide to withdraw your offering, you are required to write off the deferrable costs before any action to "start over" is initiated. However, if the offering is merely postponed - not withdrawn - and restarted within 90 days, then the deferred costs can be charged against the gross proceeds.

Future expenses. The future costs attributable to being a public company must also be taken into account. The company will be required to file current and periodic reports with the SEC that will involve legal, and accounting costs. Most companies also distribute a glossy annual report and solicit proxies for annual shareholder meetings. An ongoing investor relations program is also advisable. Executives will likely need to spend a significant amount of time on all of these matters. In addition, the CEO and the CFO will need to file certifications as to the accuracy of the financial statements contained in the SEC filings. The company will need to maintain its internal controls over financial reporting which may mean hiring additional employees or outside consultants. You may be required on an annual basis, to have the company's auditor perform an engagement to attest to the effectiveness of the company's internal controls over financial reporting (see [Chapter 9](#) for additional information).



Chapter 5. The underwriters

Your primary goal when your company goes public is a successful offering.

A successful offering not only brings a fair price for your stock, but also leads to a stable or rising price for the stock after the IPO (in the aftermarket). While there is nothing to prevent you from conducting your own public offering, the use of an underwriter, which is invariably an SEC registered investment banking firm, can help ensure that the offering is successful.

If you were to conduct your own offering, you would probably find it very difficult to find a sufficient number of buyers for your stock. The key reason for using underwriters is that they can develop a marketing structure (the underwriting syndicate) to sell the stock. The syndicate has access to buyers, who are their clients. Underwriters are also familiar with market conditions; they know the level of interest of institutional and individual investors regarding new stock issues and are familiar with the prices of stock for similar companies. They are typically in the best position to advise you on what price to ask for your stock, as well as on when to sell it. Their sponsorship usually continues well past the IPO and may affect the way your stock performs in the aftermarket.

Most companies approach an investment banker (or vice versa) a year or two in advance.

Selecting an underwriter

A group, or syndicate, of underwriters normally conducts IPOs. Your company needs to select the lead underwriter (or underwriters) who will form this syndicate.

Underwriters come with various backgrounds and have differing preferences for the kinds of companies they want to support. Some are national firms that seek out companies with national reputations and established growth records. Others are regional firms that prefer companies from their geographic area or in certain industries like health care or computer software. Others will specialize in so-called “penny stocks.”

Ideally, you will have already developed a relationship with an investment banker by the time you decide to go public. Most companies approach an investment banker (or vice versa) a year or two in advance. Some start-up companies make this connection during early-stage private placements; in so doing, they avail themselves of the investment bankers’ advice on positioning their companies to go public. Investment bankers may assist in arranging financing in those years, keep you informed of current and predicted general market conditions and the mood of the market with regard to your industry, and advise you on the appropriate time to go public.

If you do not already have an investment banker, there are many things to consider when searching for one. It is important to keep in mind that your relationship with your investment banking firm will likely not end when your IPO is completed. Because it may be an ongoing relationship, you should make your choice with all the care you exercise in selecting your auditor, accounting advisors, attorneys, and the other professionals with whom you work.

Investment bankers, unlike other professionals, do not typically charge hourly rates for their services. You compensate them through commissions on any completed deals they package for you. These commissions do not usually vary significantly from firm to firm, so pick from the best firms available.

An effective way to begin to consider which investment banker you may wish to approach is through a mutual contact (your directors, investors, accounting advisors, or attorneys may be able to assist you). Investment bankers are typically not very responsive to unsolicited letters, especially if they suspect that they are form letters sent to every investment banker in the area.



Be prepared to shop around and compare firms. If your company has promise and the investment bankers know you are talking to other firms, they may show greater interest and be more competitive. In such circumstances, the selection of underwriters is referred to as a bake-off. Here are some characteristics to look for in investment bankers:

Reputation

In an IPO, the underwriters' reputation is of great importance. Institutional and individual investors may have greater confidence in your stock, if a highly regarded investment banking firm is named in your prospectus as the lead underwriter.

Reputation can also affect the lead underwriter's ability to organize a strong syndicate of other underwriters to assist in selling and distributing the stock.

Distribution capability

You will want the underwriters to distribute your stock to a client base that is sufficiently strong and varied to generate ongoing market interest in the stock after the IPO. Investment banking firms have wide client bases. You should understand the composition of the client base and evaluate it in the context of your strategy.

Some firms have access to many institutional investors, while others emphasize individual or "retail" investors. Some have an international emphasis, while others are domestically oriented. Evaluate the quality of their clients, whether they are long-term investors or speculators. Normally, when the underwriters access their own clients and a strong syndicate to distribute your stock effectively, it will be more likely to show strong price performance in the aftermarket. You should always ask any proposed lead underwriter what the aftermarket performance of their IPOs have been in the recent past.

Calendar

You should ask any prospective lead underwriter what other offerings are on their "calendar" of offerings. These other offerings will be competing with your IPO for attention from the people at the lead underwriter responsible for the actual allocation and placement of your shares. It is extremely important that your offering receive sufficient attention during the last week or two prior to the pricing of your transaction.

Experience

The investment banking firm should typically have experience in underwriting issues of companies in the same or similar industries. This may influence its ability to price the issue accurately and may give it improved credibility when explaining and selling the company to the public (see Table 5-1 "Lead Managers").

Market-making capability

Once the stock has been issued to the public, the lead underwriter generally assumes responsibility for continued sponsorship of your company in the financial community. This sponsorship includes "making a market" in the company's stock and assisting the company in sustaining public interest in the stock by providing ongoing progress reports to securities analysts and organizing presentations to investor groups. Other members of the syndicate may become market makers as well.

Table 5-1 Lead Managers	2008		2009		Total	
	#	\$MM	#	\$MM	#	\$MM
Goldman, Sachs & Co.	6	20,628.50	16	7,366.14	22	27,994.64
JP Morgan	4	18,248.00	16	5,242.25	20	23,490.25
Credit Suisse	9	1,748.65	13	9,724.74	22	11,473.39
Morgan Stanley	3	1,072.60	16	6,532.56	19	7,605.16
Santander	0	-	1	7,036.73	1	7,036.73
Citi	6	2,001.25	7	2,197.78	13	4,199.03
BofA Merrill Lynch	0	-	11	4,175.85	11	4,175.85
Merrill Lynch & Co.	9	3,204.60	2	180.00	11	3,384.60
Barclays Capital	0	-	5	1,436.25	5	1,436.25
Deutsche Bank Securities	1	130.00	3	1,046.20	4	1,176.20

* Full credit given to each lead manager on the transaction.

* Data is based on U.S. common stock new issues, excluding closed-end investment funds, and proceeds offered into all markets, excluding over-allotments.

The market makers in the stock trade in your stock, offering firm prices to buy or sell shares. The lead underwriter generally serves as the principal market maker. In order to maintain a market, the lead underwriter may need to devote a sufficient amount of capital to take large positions (i.e., short or long) in your stock. Without this support, large shareholders may not have much liquidity, interest may wane, and the market price of your stock may suffer. When you consider the aftermarket performance of the proposed lead underwriter, you are often assessing its willingness to place its capital at risk for its client companies.

Research analysts

The financial community will look to the lead underwriter as a primary source of information about your company. Therefore, the selected investment banking firm should have experienced analysts, respected by the financial community, and closely following the industry in which the company does business.

Effective July 29, 2003, the SEC announced conflict of interest rules between research analysts and their investment banking firms. The rules are designed to promote independence and objectivity of research. Research analysts often actively participated in the road show and other marketing activities; that no longer happens. But that does not reduce the importance of having experienced analysts who are respected covering your company.

It is highly advisable to seek advice of counsel familiar with these and other SEC regulations in order to be fully aware of their implications and your company's resulting obligations.

Ability to provide financial advice

During and after your IPO, you will look to your investment bankers for financial advice. You may need help in obtaining additional funding in the future, advice on potential mergers and acquisitions, or insight into the investing public's attitude toward your company.

Other considerations

You should talk with the proposed investment banker's other corporate clients to find out firsthand what their experience has been and how they feel about their relationship with the

underwriter. You should ask both about working with the underwriter during the offering and how supportive the underwriter has been after the offering. Read the prospectuses of other IPOs in which the investment banker has acted as the lead underwriter. You should also take the time to be sure you are comfortable not only with the people with whom you will be initially directly involved, but also with those who will have ongoing responsibility for market making, research, and sales sponsorship. The personal chemistry between your investment bankers and you, your management team, and your Board of Directors is extremely important. You may also consider using more than one lead underwriter. A company may choose to use two or more underwriting firms to co-manage its offerings if the company has a good relationship with more than one firm or if the company sees advantages to combining the client bases, research capability, geographic strengths, and other resources of the underwriting. Remember that there are conflicts of interest between you and the underwriters. They have long-standing relationships in particular with their institutional customers and they are paid only if the transaction is completed, whether successfully or not in the aftermarket.

What underwriters look for

Before any underwriters agree to proceed with your IPO, they will want to investigate your company to decide whether they want to take you public. This investigation constitutes a portion of their due diligence (they will also do specific due diligence on the registration statement later in the process). Assuming they decide to back your company, the information they gather during their investigation will also assist them in determining how to price the stock. The underwriters may closely investigate many of the items described in [Chapter 2](#) under "Is your company ready," including management quality, product quality and industry potential, earnings history and potential, company reputation, and financial position.

The underwriters' investigation can take several weeks, depending on their familiarity with your company and your industry. They will quiz your key executives, and they will talk to people outside the company, including customers, suppliers, competitors, and people who are knowledgeable about the industry.

A written business plan is extremely helpful in providing information about your company to the underwriters. It should include a realistic portrayal of your company's operations, strengths, and weaknesses and of the projected application of an offering's proceeds. A well done business plan also provides a lot of information that will be useful when drafting the registration statement. A detailed and

The underwriters may investigate management quality, product quality and industry potential, earnings history and potential, company reputation, and financial position.

thorough business plan can reduce the time and expenses incurred by attorneys and other professional advisors.

Remember that even if the underwriters complete this initial investigation to their satisfaction, they will have no legal commitment to take you public until the completion of the marketing, which is one of the last steps in the IPO process.

The underwriters will also evaluate factors related to the offering itself in determining whether to take you public. These include:

Use of proceeds. The underwriters will evaluate how much money you will need to effectively generate larger future profits. If you require more money than can realistically be raised in the public market at the time, it may be wise not to try to go public now. If a large amount of the proceeds will go to shareholders or if key employees are selling stock, the underwriters may want some assurance that these people are not selling because they have lost confidence in the company (i.e., that the offering is not a “bailout”).

Marketability. The underwriters will also consider the state of the markets at the time, both generally and for a company in your industry and at your stage of development. These things can change quickly, so you must be prepared to be flexible in this process.

Selecting a trading market

Working with your lead underwriter and legal counsel, you should consider on what trading market you want your stock to trade after the IPO. Newly issued stock is most often traded on an OTC basis, with many issues going straight to the NASDAQ. Many new public companies may not be able to meet the listing requirements of the NYSE, which requires United States (U.S.) companies to have, among other things, at least 1,100,000 publicly held shares, an aggregate pretax income of at least \$10 million for the last three fiscal years with a minimum of \$2 million in each of the two most recent years, and at least 400 round lot (100 shares) holders.

While the exchanges operate as auction markets, the OTC market generally conducts business by negotiation. Broker-dealers contact each other and negotiate the bid and asked price. The bid side represents the price at which a security can be sold; the asked side represents the price at which a security can be purchased. People who wish to buy or sell an OTC security ask their broker to get bid-asked prices. If the transaction is a large one, the broker calls several other broker-dealers (the “market makers”) for this information and reports back the best price obtainable. NASDAQ is a blended OTC market, because the bulk of the trades on NASDAQ are

The financial community will look to the lead underwriter as a primary source of information about your company.

done electronically through traders looking at the various bid and asked quotes from market makers.

Most companies whose stock trades in the OTC market will seek inclusion in the NASDAQ, which provides price and volume information and helps support a trading volume through its dealer network. The NASDAQ is comprised of three tiers with approximately 3,200 companies. They are referred to as the, “Global Select,” the “Global Market,” and the “Capital Market.” The requirements for inclusion in the NASDAQ Global Market listing include having at least 1.1 million public shares with a market value of \$8 million or more and at least 400 round lot holders.

The listing requirements of the NYSE and the NASDAQ are detailed in Appendix C. In addition, both the NYSE and NASDAQ set forth independent corporate governance requirements for companies trading on or through them. See “Corporate Governance” in [Chapter 4](#).

Types of underwriting

There are generally two types of underwriting:

A firm commitment. Under this arrangement, the underwriters agree to buy all the stock being offered at a fixed price, usually determined in close proximity to the date the registration statement becomes effective. They then resell the stock to the public. If they are unable to resell all of the stock, they must still buy the stock and keep it until they can resell it later.

The firm commitment is the best and most common arrangement, since it ensures you that your company will receive a certain sum of money by a certain date. It also facilitates listing on an exchange, since the lead underwriter makes a representation to those organizations as to the distribution of the offering. The next choice arrangement may be the all or none agreement, a variation of the best-efforts arrangement described below. This puts the risk of sale on you, but at least assures you that you will not go public, unless all the stock is sold. With a strictly best-efforts arrangement, the amount of money you receive may fall significantly short of your needs while burdening the company with all the requirements of being a public entity.

The type of underwriting that is offered to you will depend on the underwriting firm that you are using and the nature of your stock offering.

A best efforts commitment. Essentially, the underwriters agree to use their “best efforts” to sell the new issue on your behalf. If they do not sell the entire amount to the public, they have no obligation to purchase the balance. Thus, they are acting merely as your agent. These are rare in IPOs and are practically impossible to do in any offering that will be listed on an exchange or on NASDAQ.

There are many variations of the best efforts commitment. Under “all or none” agreements, the underwriters will either sell the entire issue or cancel the whole offering and return the purchase price to investors who paid for part of the issue. Other agreements call for a minimum number of shares to be sold (i.e., the underwriters and the issuer may agree that two-thirds of the shares will have to be sold for the offering to be completed, after which the remaining one-third will be sold on a strictly best efforts basis).

The type of underwriting that is offered to you will depend on the underwriting firm that you are using and the nature of your stock offering. If one of the major firms agree to underwrite you, it will almost always agree to a firm commitment. The smaller firms that handle more speculative offerings will generally do so on a best-efforts basis.

Pricing the stock

As in most pricing situations, no set formula exists for determining the proper price for a company’s stock. Invariably, the pricing for an IPO is determined by a combination of factors. Your investment banker will examine the total market value of the companies that operate in your field. If none exist, the underwriters will then try to find other companies in related areas. They will examine price-earnings ratios, capital structure, debt-to-equity ratios, return on assets, return on sales, etc., of these companies. They will weigh carefully your prospective earnings and dividends based upon past experience, the amount of stock that will be available, and the potential demand.

If possible, it will be useful for you to perform this analysis of other companies prior to meeting with underwriters on price. It is a good idea to develop a valuation model well in advance of the IPO (e.g., more than one year in advance) and use this information to refine the business model to maximize

the long-term valuation. In addition, this valuation model may be useful in pricing employee stock options. There is usually a good deal of information available about companies similar to yours to help you develop a range for the price of your stock. This analysis will help you negotiate realistically with the underwriters. If your company is selling stock to the public for the first time, pricing may be entirely different than for a company that has had its stock sold on an exchange for several years. Cautious buyers may want to wait and see how your company’s stock behaves before they purchase it, reducing demand. If your company is not well known or operates only locally, this factor will be weighed in setting the offering price.

It is also possible that, although your company is not well known in comparison with others in your industry, your growth patterns and potential are so attractive that the public will accept a greater price-earnings ratio for your company’s stock than for others that are more seasoned. Ultimately, the price for the offering will principally be a function of the demand for the stock during the marketing period, as evidenced in the book building process that the lead underwriter has led. If demand has been particularly high, it may be possible for the company to increase the size of the offering or the expected price. Alternatively, if the market has weakened or demand is not as high as expected, the expected price may have to be cut.

It is not necessarily advantageous for your stock to be sold for the highest possible price that underwriters could seek. If the IPO price is set too high in relation to the company’s record, industry, and market conditions, the aftermarket may be weak. Consequently, underwriters usually advise you to sell slightly (up to 15%) below the anticipated aftermarket price. For IPOs in 2008 and 2009, the average increase in share price one day after the offering was 6.4% and 9.7%, respectively.

Sometimes, a stock’s price will increase sharply immediately after the IPO. This does not mean that the stock was priced incorrectly. Underwriters try to establish a price under normal trading conditions. Sometimes, though, speculative surprises occur. There have been instances where the trading price has doubled or tripled in the first few weeks of trading. For 2008, the greatest first-day gain experienced was 142.9%. For 2009, the greatest first-day gain experienced was 33.5%. IPOs generally experienced more moderate first-day gains in 2008 and 2009. The IPO market was substantially impacted by the financial crisis in 2008 and so its results are not necessarily comparable.

There is an alternative method of marketing and pricing an offering that can be used that does not involve the book building process described above. This is a dutch auction.

Unlike traditional IPO pricing, this arrangement is based on a transparent bidding process, where the bidding can be done over a three-to-five-week period by individual investors instead of through a nontransparent book building process run by a lead underwriter. The pricing demand is based on the bids made by auction participants with the lowest price that can sell the total number of shares setting the price for all of the shares. This method has greater risk to the company, since it does not allow the underwriters to effectively plan to establish an effective aftermarket (which the lead underwriter does in a traditional IPO), but it is a less costly offering process alternative since the underwriter generally does not receive the same magnitude of commissions. Some underwriters, who sponsor these offerings, also suggest that it could lead to a higher initial offering price, though this may be at the expense of the immediate aftermarket performance. If you are considering this type of IPO, you should carefully discuss the advantages and disadvantages with your advisors.

Size of the offering

Determining the appropriate offering size is important, as it may impact the company's engagement of an investment bank and the ability to attract high-quality investors. If the offering is not large enough, many institutional investors will be hesitant to invest due to the potential lack of an ability to quickly liquidate their positions. The median transaction size for issuers in 2008 and 2009 was \$103.2 million and \$130.3 million, respectively. An offering in this range would usually translate into 5 million to 10 million shares being offered, which should be sufficient to obtain broad distribution and provide liquidity in the aftermarket. Table 5-2 shows a breakdown of the numbers of shares for offerings done during calendar year 2008 as compared to the breakdowns of the numbers of shares for offerings done during the calendar year 2009.

Table 5-2: Number of shares for

Number of shares	% of offerings	
	2008	2009
20 million or more	13.2%	30.4%
15-19.9 million	10.5	1.8
10-14.9 million	26.3	23.2
5-9.9 million	23.7	32.1
1-4.9 million	21.0	10.7
Less than 1 million	5.3	1.8

Sometimes, a company will decide that it does not need that much money. Subsequently, a partial secondary offering, in which the existing shareholders sell some of their shares, may be required to obtain the desired number of shares to be sold. In general, early-stage companies are not encouraged to make secondary offerings of any significance. If these companies want other people to invest in them, the existing shareholders must show confidence in the potential of the stock. Underwriters may become concerned if they see investors who may have held stock for only a short time and already want to sell. As for management and key directors, sales of less than ten percent of any one individual's stock may be acceptable. Of course, the underwriters may make exceptions if there are valid reasons and the sales are not perceived to be a bailout.

The number of shares is a function of price and total valuation of the company. Issuing too many or too few shares can unfavorably alter the share price and thus the total amount to be raised in the offering.

Keep in mind that underwriters have some flexibility on this matter at the time of the offering, as they are generally allowed to offer and sell ten percent to 15% more shares than promised in the underwriting agreement. This option is referred to as the over-allotment option or a green shoe and is described in more detail in [Chapter 9](#).

Table 5-3 shows a breakdown of the initial price for offerings done during 2008 compared to the breakdown of the initial price for offerings done during 2009. Underwriters typically like to price the offering near the \$10-\$20 range in order to allow 100 share round lots to be priced in a range that facilitates the participation of more retail investors.

Table 5-3: Initial price for offering

Number of shares	% of offerings	
	2008	2009
\$20 or more	15.1%	10.5%
15-20	33.3	18.4
10-15	32.9	39.5
5-10	16.9	26.3
Less than 5	1.8	5.3

Chapter 6. Registration

The entire IPO process revolves around your company's registration with the SEC.

This registration is achieved through the filing of a legal document referred to as the registration statement, the required general contents of which are governed by the 1933 Act.

The preparation of this statement can be a lengthy process, and even if the process goes smoothly, covering all of the steps can take three to four months, and often longer for foreign filers. During this period, a series of planning and review meetings (often referred to as all hands meetings) are held with company officials, the company's counsel, the underwriters and their counsel, and the company's external auditors. At these meetings, an initial timetable is established, responsibilities are assigned, the components of the registration statement are discussed, the amount and use of proceeds are estimated, financial and legal information is presented, registration statement drafts are reviewed, and other aspects of the offering are assessed. (Note: A typical timetable for a public offering is contained in [Appendix D](#).)

The lengthy timetable is, to a significant degree, governed by legalities, and your counsel will handle the majority of the details associated with this registration. All the parties involved, however, are subject to civil and criminal penalties under the 1933 Act for misstatements or omissions in the registration statement and prospectus. Each member of the IPO team is responsible for performing his or her own due diligence or investigation to ensure the accuracy of statements in the registration statement.

As noted in [Chapter 1](#), when completed, the preliminary registration statement is filed with the SEC. After the registration statement is filed, the SEC typically reviews it for the compliance with the disclosure and accounting requirements and sends out a comment letter (which can be lengthy). In virtually all cases, the registration statement must be revised to respond to the comments. The company must make the necessary modifications by filing amended versions of the registration statement until the SEC is satisfied and declares the registration statement effective. The SEC staff has issued a [Financial Reporting manual](#), as well as "[Staff Observations in the Review of Smaller Reporting Company IPOs](#)" which may be helpful to companies in preparing their initial registration statement. In the interval between the initial filing of the registration statement and its effective date (the so-called "waiting period"), the company and the underwriters may distribute copies of a preliminary prospectus. Such prospectus must bear a legend stating that a registration statement related to the offering has been filed with the SEC, but has not yet become effective and that the securities may not be sold, nor may offers to buy be accepted, before the effective date. Because this legend is printed in red ink, the preliminary prospectus is commonly referred to as the "red herring." The red herring is typically printed after the company and its advisors conclude that resolution of the remaining comments from the SEC is not likely to require material revisions to the preliminary prospectus and a new circulation to potential investors. The preliminary prospectus that is distributed will also include an expected price range for the offering.

The merits of your offering may also need to be reviewed and approved by the states where the stock is to be sold, and the underwriters' compensation must be reviewed by FINRA. Once these requirements are addressed, a final registration statement is filed, the pricing of the offering occurs, and the offering commences.

There is also an accompanying registration of the class of stock being sold under the 1934 Act; this is a very short document that incorporates portions of the 1933 Act registration statement. See [Chapter 9's](#) discussion of the 1934 Act.

Who does what

Generally speaking, the better prepared the company and its executives are in putting the registration statement together, the more efficient (and less expensive) the outside professionals can be. While each party has specific responsibilities, they also have to be comfortable that the other groups have done their assigned tasks. Everyone is



associated with the registration statement in some way; an error in any portion of the statement is potentially damaging to all parties. Here are the basics as to what is generally expected of each party:

Company management

The most important team members are the company's management team, led by the CEO and the CFO. The management team acts as a liaison between the working group and the company's Board of Directors and plays a critical role in all aspects of the IPO process. The management team will make structural and timing decisions relevant to the IPO, and with assistance from the company's advisors, will prepare the registration statement and respond to the SEC comments and make the road show presentations.

The best way for executives to expedite the process is to have a detailed and up-to-date business plan ready for all the outside professionals to use as a reference. The plan normally includes not only the company's plans for the future, but also analyses of the company's place in its industry, details about its market, an assessment of the competition, a complete description of its products or services, and consideration of weaknesses in the company's performance. Management must also be ready to certify to the accuracy of the financial statements and effectiveness of the company's internal controls as part of the annual reporting process as well as to all the disclosures included therein.

Company counsel

As the registration statement is a legal document, the attorneys generally take the lead in drafting the registration statement. When they have questions and need information, they call the company's management. On the basis of the information gathered, counsel's role will be to assist the company in deciding which particulars should be included in the registration statement (i.e., what facts are material) and how they should be included. Additionally, counsel will file the registration statement with the SEC and coordinate, assist in the drafting of, and file responses to the SEC comments on the registration statement. The company's counsel is also responsible for assisting the company with its pre-IPO corporate housekeeping and IPO preparations, helping the company coordinate the due diligence process, negotiating the underwriting agreement on behalf of the company, issuing a legal opinion on the validity of the securities being offered, and seeing that the registration statement is complete and not misleading, and advising the company on securities-related matters.

Auditors

The company's auditor must report on the financial statements included in the registration statement. This means that the auditor must audit the financial statements and render a report on the audit. As noted previously, if the company's financial statements have been audited on a regular basis in the years leading up to the filing of a registration statement, the company's tasks associated with completing the financial statements in SEC-required form may be less difficult. Additionally, subsequent to registration, the auditor may be required to issue an opinion on the company's internal controls over financial reporting (see [Chapter 9](#) for additional information). The auditor will also review drafts of the registration statement for accuracy and consistency of financial information. Additionally, the auditor will assist in the resolution of financial reporting questions raised by the SEC during the SEC review process and will issue comfort letters to the underwriters as part of the due diligence process.

Underwriters

As previously noted, the lead underwriter will form an underwriting syndicate, provide advice on the pricing and timing of the issue, ensure demand for the securities by promoting them, and organize the road show in which the company is presented to potential investors. It will also participate in the drafting sessions for the registration statement and in responding to the SEC's comments.

Underwriters' counsel

The underwriters appoint legal counsel whose principal role is to do its best on behalf of the underwriters, to confirm that the registration statement is complete and not misleading. The underwriters' counsel will review the registration statement and related exhibits, conduct due diligence meetings, draft the underwriting agreement, and request comfort letters from the auditors. They will also participate in the drafting sessions for the registration statement and in responding to the SEC's comments.

The company's auditor must report on the financial statements included in the registration statement.

Due diligence

One of the reasons the actual process of putting together a registration statement may take three months or longer is that the professionals involved must be certain that all necessary disclosures have been made. This requires that a complete due diligence process be performed.

Under the 1933 Act, securities fraud liability may be incurred if a registration statement contains misstatements of material facts or omissions of material facts required to be included in the registration statement at the time that the registration statement becomes effective. The company, its directors, the officers who sign the registration statement (the principal executive, financial, and accounting officers), the underwriters, and any experts (such as auditors) participating in the registration may all be potentially liable. The company itself is liable for any material deficiencies, regardless of good faith or the exercise of due diligence.

Due diligence is the process of ensuring that the information in the registration statement is accurate in all material respects and that the registration statement does not contain an untrue statement of a material fact or omit to state a material fact required to be stated in the registration statement or necessary to prevent statements in the registration statement from being misleading. One component of due diligence consists of the professionals questioning key management personnel about company activities, matters disclosed in the prospectus, and matters not disclosed in the prospectus. Here are some of the principal issues that must be dealt with:

with the company, indemnification agreements, and the number of shares owned of record and beneficially (shares in which they, directly or indirectly, have or share voting or investment power). In some cases, the individual directors and officers may be interviewed by your advisors.

Financial statements

The audited financial statements will be included in the prospectus with reliance on the auditor's report given on the authority of the auditors as experts in auditing and accounting. In order for a company to include the accounting firm's report in the filing and to refer to the firm as experts, the company must request and obtain the auditor's consent to the inclusion of their report in the prospectus and to being named as experts. Before these consents are given, the auditors must perform a reasonable investigation through the filing dates, performing a subsequent events investigation to determine whether the financial statements and their opinion thereon are still appropriate.

This investigation includes inquiries into any events that occurred or became known after the date of the auditor's last report which, had they been known at the time, would have been disclosed or reflected in the financial statements. The auditor's review and discuss with management any concerns they may have with the interim financial statements. They also read the entire prospectus for inconsistencies between the financial and nonfinancial portions and any material matters that have not been disclosed. The auditors are also asked by the underwriters to "provide comfort" (as explained below) on certain financial amounts disclosed in the registration statement (outside of the audited financial statements).

Comfort letters

During the registration process, the underwriters and their counsel will meet with the company and its auditor to discuss the financial statements and to reach an agreement on the auditor comfort letters. In requesting these comfort letters, the underwriters are seeking assistance in performing a "reasonable investigation" of financial and accounting data in the prospectus that are not covered by the auditors' report. Two comfort letters are generally issued - one on the effective date and one on the closing date. The comfort letters list very specific procedures performed at the request of the underwriters. The auditor will generally furnish a preliminary draft to the underwriters well in advance of the first due date so that the underwriters may decide whether the procedures described in the letter satisfy their needs.

The comfort letters list very specific procedures performed at the request of the underwriters.

All significant corporate documents and related information

Your counsel and underwriters' counsel should review articles of incorporation, by-laws, minutes of board and committee meetings, major contracts, employment agreements, stock option plans, and other significant company documents to verify that the prospectus disclosures are accurate. They usually circulate questionnaires to all directors and officers, requesting comments on the latest draft of the registration statement and asking them to verify the information disclosed, including their names, prior experience, direct and other remuneration, options, warrants and rights, transactions

The procedures, performed by the auditor, usually include comparison of financial data contained throughout the prospectus to accounting records or financial statements and consideration of financial results available subsequent to the last audit for purposes of determining whether there have been any declines in sales or income or other trends that are not adequately disclosed in the document. It is wise for the company to be involved in the determination of what is addressed in the comfort letters, since management may be able to point out problems that can be resolved with the underwriters in advance of the issuance date. For example, sales for the most recent month may have declined from sales for the same month a year ago. There may be a simple explanation for this, and if you know that the comfort letter will point out this decline, you can discuss the situation with the underwriters so that the letter will not surprise them or delay the filing.

Types of issuers

There are three main types of issuers: domestic issuers, smaller reporting companies, and foreign private issuers. Domestic issuers (which are the primary focus of this publication) are generally organized under the laws of a state of the United States and have their main corporate headquarters located within the U.S. Based upon the size of the entity, certain of these issuers may qualify as smaller reporting companies. Foreign private issuers are the third type of issuer. The SEC offers certain financial statement and disclosure accommodations to foreign private issuers.

Chapter 10 defines foreign private issuers and summarizes some of the most important of these accommodations. You should consult with your legal counsel to determine if your company may qualify as either a smaller reporting company or a foreign private issuer.

The registration statement

Most registration statements for IPOs of domestic issuers are prepared on Form S-1, which can be used by any issuer. There are scaled disclosure requirements for smaller reporting companies.

The registration statement consists of two principal parts. Part I is the prospectus, the legal offering document, normally prepared as a brochure or booklet for distribution to prospective buyers. The prospectus also serves as a marketing document for the IPO. Part II contains other detailed information. The registration statement is available for public inspection at the office of the SEC, or on the SEC's website, www.sec.gov.

The following discussion focuses on the Form S-1 registration statement. Consult with your legal counsel regarding the specific requirements of each part of the registration form.

Part I: The prospectus

The registration forms contain a series of detailed "items" and instructions, in response to which disclosures must be made. Because the prospectus is the selling document, it is usually written in narrative form and is highly stylized. The SEC requires the use of "plain English" for parts of the document (the cover page, summary, and risk factors sections) and encourages it for the whole document. The plain-English rules require the use of short sentences that avoid technical and legal jargon. The SEC also emphasizes the necessity of carefully organizing information in the prospectus in a logical sequence and presenting that information in an easy-to-read, understandable manner.

The prospectus serves two potentially conflicting purposes. On the one hand, as the basic sales brochure for the stock issue, it should present the best possible image. On the other hand, to protect the company, controlling persons, directors and officers, and underwriters from potential liability under the 1933 Act, it should not be written with the flair and style of marketing literature. Its emphasis should be on adequate disclosure and, while you will highlight all the positive aspects of your company, you should also bring out the negative aspects. Read prospectuses of other companies in your industry; this will prepare you for your own first draft and its reference to the risk factors and potential weaknesses associated with your company. Investors are accustomed to reading prospectuses and understand that they are not sales pitches.

In practice, the information in the registration statement is usually presented in the following order (note that there are scaled disclosure requirements for smaller reporting companies).

Cover page. The outside front cover provides key facts about the offering, including the name of the registrant, the title and number of shares of the securities to be sold, a distribution table (the price to the public, the underwriters' discount, net proceeds to the company, and net proceeds to selling shareholders on per-share and aggregate bases), and the date of the prospectus. At the time of the red herring, the cover page will list a range of per share prices, such as "It is currently estimated that the initial public offering price will be between \$12 and \$14 per share," and the distribution table will be blank. The inside front or outside back cover includes a table of contents, and information regarding the distribution of prospectuses.

Prospectus summary. This section of the prospectus highlights the salient features of the offering and may include brief descriptions of the business, the offering, the use of proceeds, and risk factors. It will also disclose summary financial information. A good deal of time will be spent in preparing this summary, as it will often serve as the basis for a potential investor's decision to consider the stock further.

The company. An introductory statement about the company is generally given, explaining what business it is in, its main products, when it was formed, and where it is located. This is often included in the prospectus summary.

Risk factors. The prospectus includes a discussion of the most significant factors that make the offering speculative or risky. These may include such things as a lack of operating history, an accumulated deficit, operating losses in recent periods, an expectation of future losses, uncertainty of market acceptance of the product, dependence on key personnel or certain customers, competition, dependence on expansion of the organization, such as sales, support or production, and technological change. "The issuer should place any risk factor in context so investors can understand

the specific risk as it applies to your company and its operations." As other sections of the prospectus are written, be alert for issues that should be highlighted in the risk factors section.

Use of proceeds. This section describes the purpose of the offering, explaining how the funds will be spent, such as to reduce debt or acquire a new business, and must be carefully drafted. The SEC "requires a first-time registrant to report the use of proceeds in its first periodic 1934 Act report (quarterly report or annual report, whichever is filed first) after effectiveness, and thereafter in each of its periodic 1934 Act reports until the registrant has disclosed the use of all of the proceeds or disclosed the termination of the offering, whichever is later."

Dividend policy. The company's dividend history and any restrictions on future dividends are explained. Many companies have never paid dividends, retaining all earnings to finance continuing operations and expansion. Any intent not to pay any dividends in the near future must be disclosed.

Capitalization. Although not specifically required by the SEC, this section contains a table exhibiting the capital structure (debt and equity) of the company before and after the offering. (i.e., on a pro forma basis).

Dilution. When substantial disparity exists between the IPO price and the book value and price that was paid for existing shares owned by officers, directors, and major shareholders, the resulting dilution of the purchaser's equity interest is shown. This is normally done through tables that compare the price paid by new investors with that paid by existing investors and the net tangible book value of the stock with the price paid by new investors.

Selected financial data. This section includes certain selected financial data for each of the last five fiscal years or from the date of the company's inception, if shorter, and any interim periods that are included in the financial statements. The purpose is to highlight certain significant trends in the company's financial condition and its operations. Consequently, the data generally includes revenues; income (loss) from continuing operations, in total and per share (in practice, many companies disclose most of the details contained in their statements of operations); total assets; long-term obligations (e.g., debt, capital leases) and redeemable preferred stock; shareholders' equity; and cash



dividends declared per share. A company may also include additional items which it believes would enhance an understanding of and highlight other trends in their financial condition and results of operations.

There is no requirement for a smaller reporting company to present selected financial data, although the underwriters may request a smaller reporting company to include it.

Selected quarterly financial data. There is no requirement to provide selected quarterly financial data within an initial registration statement. However, your underwriters may ask you to include this quarterly financial data to provide more information to potential investors. You should discuss this with your underwriters early in the process as the accumulation of this data may be time consuming. After the initial registration statement is declared effective, the company must be prepared to include selected quarterly financial data within its subsequent filings with the SEC.

Management's discussion and analysis (MD&A) of financial condition and results of operations.

Management is expected to explain its results of operations and financial conditions and highlight trends, that may be reasonably expected to affect the future. Management should disclose critical accounting policies, significant estimates made, any trends, commitments, or events that may affect working capital, commitments for capital expenditures, and the source of funds for those expenditures. Significant changes from year to year in line items on the income statement should be explained and significant related-party transactions should be discussed. Anticipated liquidity and capital resource issues should be discussed, including future material capital expenditures, significant payments due on obligations, discretionary payments, acquisitions requiring cash financing, and other commitments. Any identified material deficiency in short- or long-term liquidity, as well as the proposed remedy or the fact that the deficiency has not been remedied should be disclosed. Off-balance sheet arrangements that have, or are reasonably likely to have, a current or future effect on various aspects of the business should also be disclosed. Contractual obligations should be shown in a table showing future payments for certain contractual obligations. Management is also expected to discuss the operations, historical results, and known trends and conditions that will, or could, affect operations.

Market risk. This section requires quantitative and qualitative information about the market risks to which the company is exposed, with a distinction being made between instruments entered into for trading or speculative purposes and those entered into for hedging and other purposes. Categories of market risk include interest rate risks, foreign currency exchange rate risk, commodity price risk, and other relevant market rate or price risks. This disclosure may be provided in a variety of formats.

There is no requirement for a smaller reporting company to present market risk, although the underwriters may request a smaller reporting company to include it.

Description of business. This section is usually the longest in the prospectus. It is intended to provide the reader with material information essential to the evaluation of the company's products and industry. Disclosures should include, but are not limited to:

- the company's historical development over the past five years and earlier periods if material
- a plan of operation for the next year
- statement regarding the period of time the proceeds from the offering will satisfy cash needs and whether it will be necessary to raise additional cash in the next six months
- principal products produced or services provided
- principal company markets and methods of distribution
- status of any announced new products under development
- sources and availability of raw materials
- customer service and support
- patents, trademarks, licenses, franchises, and concessions or other intellectual property held
- extent to which the business is or may be seasonal
- working-capital practices (e.g., if you are required to carry significant amounts of inventory to meet rapid delivery requirements or if you provide extended payment terms to customers)
- dependence on one or a few customers
- dollar amount of firm backlog
- government contracts
- competitive conditions in the business
- research and development expenditures during the last three years, including those funded by others
- environmental matters
- number of employees
- revenue, a measure of profit or loss, and assets by segment and by geographical area
- export sales
- facilities, both owned and leased
- pending legal proceedings

Management and certain security holders. This section should provide background information about management personnel and major shareholders and their financial relationship with the company. Specifically, you must provide:

- the names and ages of the directors, executive officers, significant employees, their business experience, their remuneration (including stock options, perquisites, and other indirect amounts), and any employment or severance agreements
- a description of the involvement in certain types of legal proceedings by a director, nominee for director, or executive officer during the past five years (this was amended in December 2009 to 10 years, effective February 28, 2010)
- a compensation discussion and analysis section which provides the material factors underlying compensation awarded to, earned by, or paid to executive officers in order to give the investor the information needed to understand the compensation policies and decisions made by management, including how the specific compensation elements are determined
- tabular schedules of compensation for the executive officers, among the most notable are the summary compensation table, the grants of equity-based awards outstanding at the end of the year and the options exercised and vested schedules
- Tabular schedule of director compensation
- a description of all stock option and other employee benefit plans which provides clear, concise, and understandable disclosure of all plan and non-plan compensation awarded to, earned by, or paid to the named executive officers and directors
- the stock holdings of officers, directors, and any shareholders who beneficially own more than five percent of any class of stock
- certain transactions between the company and its officers, directors, and principal shareholders
- loans by the company to officers or directors
- transactions with promoters, if the company has been in existence for less than five years

Smaller reporting companies are permitted to provide less information concerning executive compensation.

Description of securities. This section gives the par or stated value; explanations of dividend rights and voting, liquidation, and preemptive rights; and the transferability of each class of stock. It also describes any provision of the company's charter or by laws that would have the effect of delaying, deferring, or preventing a change in control of the company. Any outstanding warrants or registration rights should also be disclosed.

Information about underwriters. This section should explain the plan of distribution for the offering and where the stock will be traded after the IPO. The various underwriters in the syndicate must be disclosed, as well as the number of securities to be purchased by each. The underwriters' obligations, indemnification by the company, and any material relationships between any of the underwriters and the company should also be disclosed. In addition, any lock-up arrangement, whereby shareholders agree not to sell their shares for a period of time after the offering, is described here.

Other. Other information should include identification of the law firms finding legal opinions, the identification of experts, and the availability of additional information.

Financial statements. The last section of the prospectus will normally be the financial statements. Form S-1 requires the following:

- audited balance sheets as of the end of the last two fiscal years and audited statements of operations, cash flows, and changes in shareholders' equity and comprehensive income for the last three fiscal years, including footnotes to those statements (smaller reporting companies have different requirements — see below).
- unaudited interim financial statements (covering three-, six- or nine-month periods subsequent to the company's latest fiscal year), as well as statements for the corresponding interim period of the preceding fiscal year, if the registration statement will not be filed/declared effective within 135 days subsequent to the company's most recent fiscal year end

Smaller reporting companies are required to provide balance sheets, audited statements of operations, cash flows, and changes in shareholders' equity as of and for the two most recent fiscal years in annual financial statements. The primary determining factor for eligibility as a "smaller reporting company" is that the company has less than \$75 million in public float as of the last day of its most recently completed second fiscal quarter. When a company is unable to calculate public float, such as where no market price for its outstanding common equity exists at the time of the determination, the eligibility requirement will be less than \$50 million in revenue in the last fiscal year.

Currently, the financial statements in an S-1 for domestic registrants must be prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). However, in November 2008, the SEC issued its proposed International Financial Reporting Standards (IFRS) "roadmap" outlining milestones that, if achieved, could lead

to mandatory transition to IFRSs starting in fiscal years ending on or after December 15, 2014. Based on the progress made on the milestones, the SEC is expected to determine in 2011 whether to require mandatory adoption of IFRS for all U.S. issuers. According to the roadmap, large accelerated filers would be required to file IFRS financial statements for fiscal years ending on or after December 15, 2014, then accelerated filers in 2015, and nonaccelerated filers in 2016. An issuer's financial statements would include three years of audited annual periods in the initial year of IFRS adoption, e.g., financial statements for December 31, 2012, 2013, and 2014. The roadmap also contains proposed rule changes that would give certain U.S. issuers, based on industry and market capitalization, the option to use IFRSs in financial statements for fiscal years ending on or after December 15, 2009. As we go to press with this publication in January 2010, the SEC is assessing the comments it received on the proposed roadmap and is considering next steps. Because the proposed roadmap has not yet been finalized at this time, the transition timing set forth in the proposed roadmap may be extended or changed. Companies preparing to go public should monitor the SEC's activity in this area.

Audited financial statements of a business acquired or likely to be acquired may be required to be included in the registration statement. If your company has acquired a business within the last three years, or an acquisition is probable, calculations will need to be performed to determine if the acquisition is large enough to include the acquired company's financial statements. The size of the acquisition will also determine the number of periods for which financial statements are required. As a result of including audited financial statements of an acquired business in the registration statement, unaudited pro forma financial information reflecting the business acquisition will be required in another section of the Form S-1.

Separate financial statements of equity method investees and financial guarantors may also be required if certain criteria are met.

Refer to [Chapter 10](#) for financial statement requirements for foreign private issues.

Part II: Information not required in prospectus

Part II of Form S-1 requires, among other things, disclosures of the expenses of issuance and distribution (excluding underwriters' commissions), indemnification of directors and officers, and sales by the company of unregistered securities within the past three years. It also requires the filing of various exhibits, including the underwriting agreement, articles of incorporation and bylaws, stock

option plans, pension plans, and certain contracts that are material to the company or are specifically referred to in the prospectus (e.g., employment agreements, leases and mortgages, and key supply contracts). Companies may request confidential treatment of the material terms and provisions of certain contracts (e.g., pricing terms, royalty rates, milestone payments). If granted by the SEC, such terms and provisions are blanked out and only the redacted version is available to the public. Obtaining confidential treatment from the SEC is not an automatic process and may involve substantial discussion with the staff of the SEC, which can delay the offering process.

The "red herring"

The preliminary prospectus is typically printed after the company and its advisors conclude that resolution of the remaining comments from the SEC is not likely to require material revisions to the preliminary prospectus and a new circulation to potential investors. The preliminary prospectus is typically referred to as a "red herring," due to printing the required cautionary language on the front cover in red ink, following:

The information contained in this prospectus is not complete and may be changed. These securities may not be sold until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and it is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

The red herring prospectus may be distributed to the general public. Since it is before the pricing of the offers, it does not contain the exact offering price. However, the SEC requires that a bona fide estimated price range be disclosed. If the final pricing is outside the range set forth on the red herring that was distributed, you will have to consider if the change is a material change that requires revised disclosure to be distributed (or "recirculated") to the prospective investors. The SEC also has guidelines on this and you should consult with counsel if this occurs.

Printing and distribution of the red herring prospectus is integral to both the marketing effort and to having the SEC accelerate the effective date of the registration statement.

Printing

Some attorneys will provide printing services for the early drafts of the registration statement. After the early drafts have been discussed, it is time to go to the financial printing specialists. Only a few firms in the major cities specialize in financial printing. These printers will be alert to and aware



of changing SEC rules and regulations regarding prospectus and registration statement presentation, format, required size of type, etc. The printers will also be sensitive to your need for complete accuracy, timelines, and security. The registration statement, including all exhibits, is required to be filed on the SEC's EDGAR system. The major financial printers are set up to accommodate the EDGAR filing process. Since 1995, the SEC's EDGAR system has provided online access—www.sec.gov—to most SEC filings and may be extremely useful to you when drafting your registration statement. Through the SEC website, the company has access to previous registration statement filings, which can be used as examples in the drafting of your registration statement. Your underwriter will also supply examples of previous registration statement filings since the underwriters typically have their own preferences.

As indicated above, printing costs vary with the number of proofs and revisions (authors' alterations) made and the extent of the revisions required between the original filing and the final printing. Once the drafts are in printed form, people invariably notice details that were overlooked in the typed drafts, and every disclosure takes on new significance. Authors' alterations are very expensive; the revisions are usually requested from the printer on a quick turnaround basis, which often requires overtime. You cannot avoid revisions, since they are essential and often reflect changes in the market. With careful planning and organization, though, you can minimize them and save time, money, and a lot of frustration.

Keep everyone involved in reading the early drafts, and do as much in-house as possible in advance of forwarding your "final" draft to the printer. Color art for the inside cover of the prospectus, illustrations, and related legends, pie charts, and graphs should be prepared and approved by everyone in advance. The artwork must be just as accurate as the rest of your prospectus. For example, in one company's registration statement, it presented a four-color illustration of all its various products. The SEC questioned why one of the depicted products was not described in the prospectus and found that the product was no longer being manufactured. The result was the artwork had to be redone and reprinted.

As soon as the registration statement is declared effective by the SEC and pricing occurs, the final prospectus is printed while distribution of the prospectus is easier now, due to new SEC rules adopted in 2005, the printing of the final prospectus is done very rapidly to facilitate its distribution. Good financial printers understand your time constraints and can usually accommodate you.

SEC review

Once the registration statement is completed and filed, it will usually be reviewed by the SEC's Division of Corporation Finance to monitor and enhance compliance with the applicable disclosure and accounting requirements. The Division's staff almost always finds some deficiencies or items that it questions or believes require additional explanation. These are communicated through a "comment letter."

While the SEC may use one of three different levels of review, it is reasonable to anticipate that all IPO registration statements will receive a full cover-to-cover review by both a legal and accounting examiner. For further information on the three review procedures, refer to the [SEC staff's overview](#) of its filing review and comment letter process.

The SEC typically responds to the initial filing within 30 days by issuing a comment letter that requests clarifications and seeks changes in the registration statement and prospectus. The Company, with the assistance of its advisors, prepares a written response to each comment. The responses are typically submitted to the SEC along with a preeffective amendment to the registration statement that includes any changes made as a result of the SEC comments. Once the amended registration statement and response letter are filed, the SEC will review them and provide another comment letter. This process can involve a number of rounds of comments and additional amendments. The timing of the SEC review on the amendments can vary based on the significance of the changes and the SEC's workload at the time, but is typically within approximately 10 days.

As the comment letter process nears completion, the Company must decide when to print the red herring. If the red herrings are distributed before all substantive SEC comments are resolved, there is a risk that the SEC will require additional changes to the registration statement. Depending on the extent of the changes, there are three possible courses of action:

- If the changes are significant, it may be necessary to "recirculate" the prospectus, by distributing a revised or "stickered" preliminary prospectus to all underwriters and selling group members for delivery to possible investors.
- If the changes are not that substantial, the red herring may not have to be recirculated, but the decision should rest with counsel. These types of changes are often communicated by means of a free writing prospectus.
- If changes in the preeffective amendment are insignificant, they may be discussed with the staff over the telephone and be included in the pricing amendment.

Because of the risk of potentially having to distribute a revised –“red herring”– and the associated costs, most companies do not print their red herring until substantially all of the SEC’s comments have been resolved.

You need to reach agreement with the SEC in response to all comments before your registration statement can become effective. The road show is often timed to coincide with reaching this agreement. Final pricing discussions begin to occur just before the final amendment is filed, although the final amendment does not typically contain pricing information. Concurrent with the filing of the final amendment, companies, together with the lead underwriter, will typically file a request for acceleration of effectiveness. Final pricing discussions begin to occur just before the final amendment is filed and the pricing often occurs on the same day that the filing is made. Pricing information is generally added via a separate prospectus. The exchange (wherever the stock will trade upon completion of the offering) will also submit their approval of the company for listing or trading, as the case may be.

If the SEC grants your request for acceleration, it issues an order declaring your registration statement effective. You are usually notified by phone and are sent written confirmation by mail.

As soon as you receive notification of the effectiveness of the registration statement and pricing occurs, you should have the printer complete the printing of the final prospectus. This prospectus will have the final pricing information included and the red herring legend removed.

The thrust of the 1933 Act is adequate disclosure of information. No matter how speculative the investment or high the risk, federal law is complied with if all the required disclosures are made and not misleading.

Blue Sky and FINRA clearance

Even though you file a registration statement with the SEC, your securities must be registered under the “Blue Sky” laws of certain states where the stock is to be sold. Blue Sky is the general term applied to the states’ securities law. The name is derived from a court decision on the constitutionality of Ohio’s securities law, which prevented “speculative schemes which have no more basis than so many feet of Blue Sky.” Many states have adopted the Uniform Securities Act, which facilitates the state filing process; however, some states, like California, Texas, Illinois, Ohio, and New York, have their

own securities regulatory statutes and regulations, adding complications to the process. In order to facilitate an orderly national distribution of securities in offerings where the securities will be traded on national markets (and in certain other cases), Congress enacted the National Securities Markets Improvement Act (NSMIA) in 1996, which preempts state Blue Sky regulation for public offerings of securities to be traded on national markets.

Where NSMIA does not apply, you will be subject to the state regulations. Many states do not permit you to circulate a preliminary prospectus until you have filed their Blue Sky application forms, so the filings should be taken care of as soon as the registration statement is filed with the SEC. In contrast to the SEC, which focuses on disclosure only, some states do evaluate the “merits” of the offering and its suitability for investors in their state. The lead underwriter will generally advise you of the states in which the underwriters wish to sell the securities and the amount of securities to be qualified in each state. Underwriters’ counsel generally takes care of the filings, which vary from filing a notification of intent to sell in some states to qualifying with a registration statement in other states.

SEC regulations also call for the clearance by FINRA of the amount of the underwriters’ compensation. FINRA reviews not only the underwriting discount, but also other compensation that the underwriters are deemed to receive in connection with the offering (such as options or warrants, finders’ fees, and reimbursement of expenses normally borne by the underwriters) to determine whether the underwriting arrangements are fair and reasonable. To allow sufficient time for FINRA clearance and possible changes in the underwriting agreement that the FINRA may require, underwriters’ counsel should apply for FINRA review as soon as possible after the registration statement is filed.

The lead underwriter will generally advise you of the states in which the underwriters wish to sell the securities.

Chapter 7. Marketing the offering

The time period between the initial filing of your registration statement and the effective date is referred to as...

...the waiting period or quiet period. This is a misnomer, however, as there is a flurry of extremely important activity during this time, occupying both the underwriters and the company. It is during this period that the marketing effort takes place.

The marketing process

As soon as the registration statement is filed with the SEC, the lead underwriter begins the process of forming a group, or syndicate, of underwriting firms that agree to participate in the offering. The syndicate is formed to obtain a broad distribution of the stock and to provide a balance between institutional and individual shareholders.

In a firm commitment underwriting, the syndicate members participate with the lead underwriter in assuming the risk of selling the stock. The lead underwriter usually purchases the largest portion of the shares offered and brings into the group enough members to purchase the remainder. Each member makes a commitment to purchase a certain number of shares. When the SEC review process has reached a point that the company and the lead underwriter are sufficiently comfortable to print the red herring preliminary prospectus, the salespeople for the firms in the syndicate begin letting their clients know about the offering and furnishing them with copies of the preliminary prospectus. The syndicate may also include selling group members or dealers who agree to purchase a specific number of shares at the public offering price less a selling concession. These selling group members do not share all of the potential liabilities under the securities laws with the underwriters and as a result receive less compensation.

The selling is really a group effort. The lead underwriter "runs the books," keeping track of the outstanding indications of interest. Some participating underwriters may actually sell two or three times their commitment, and others may sell none. The company's participation through the road show is the single most important vehicle for building momentum for the offering. If momentum is strong, the lead underwriter's "book" may reflect demand that significantly exceeds the size of the offering. This is good, as it allows for some inevitable slippage in actual orders (from the number of indications of interest) and provides for continuing demand in the aftermarket.

Because the underwriting agreement is not signed until the end of the quiet period, the lead underwriter and the syndicate members know how strong the demand is for the stock before they are legally committed to purchase shares from the company. So, as a practical matter, their risks in selling the shares are limited. However, the SEC requires that each syndicate member be able to back up its commitment with sufficient capital; if the stock should not sell as well as expected, the members will be forced to purchase the full amount of their commitment (except in the event of a breach of the underwriting agreement by the company, a material adverse event impacting the company, or the occurrence of certain extraordinary market events).

As indicated previously, the underwriters have a good sense of how many shares can be sold before they enter into the underwriting agreement. Although the preliminary prospectus indicates the anticipated number of shares to be sold and the expected price range, the underwriters find out during the quiet period just how acceptable that price and offering size are to investors. Both factors may change before an offering becomes effective.

If your underwriters have done a thorough job, any changes during this period will generally reflect only changes in market conditions. Throughout the registration process, a series of pricing discussions are likely to occur between you and the lead underwriter to set the initial price and size of the offering and to apprise you of any needed revisions. Sometimes, market conditions may cool, and you may have to settle for less or cancel the IPO altogether. On the other hand, the demand for the stock may be surprisingly high, and you will be able to expand the size of the offering and/or increase the price.

The do's and don'ts of the quiet period

The 1933 Act prohibits any public offers of a security, either orally or in writing, before the initial filing of the registration statement. In this context, what constitutes an offer has been defined very broadly by the SEC and the courts. Any publicity effort, if deemed to create a favorable attitude toward the securities to be offered and to stimulate the market artificially, may lead to what is called "gun jumping" and legal problems with the SEC.

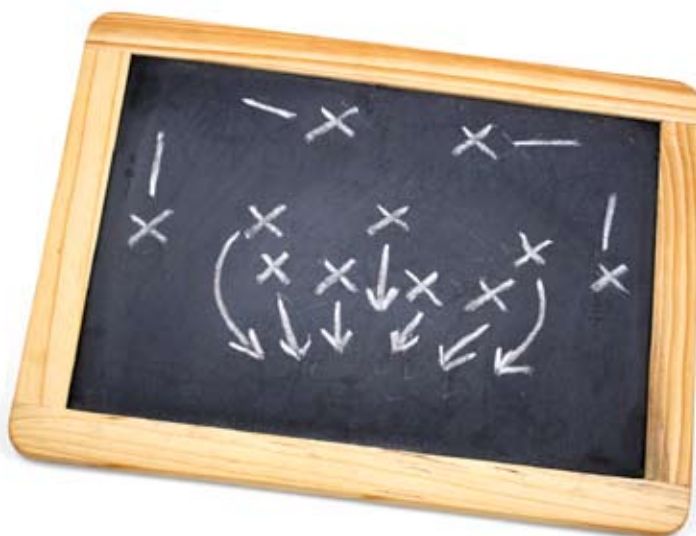
Sometimes, market conditions may cool, and you may have to settle for less or cancel the IPO altogether.

The SEC, through various releases and rules, has established guidelines for the publication of information other than the prospectus, both before and after the effective date of the registration statement. It is very important that everyone in the company be aware of these guidelines. Failure to comply can lead to a halt in the IPO process until the interest that has been stimulated has cooled down.

The practical period of time covered by the guidelines extends from 30 days prior to the filing of the registration statement to 25 days after the effective date of the registration statement, when brokers and dealers are no longer required to deliver a prospectus to potential investors (or 90 days, if following the IPO, the company is not listed on a stock exchange or certain OTC markets). During this period, any publicity release can raise questions about whether the publicity is part of the selling effort, even if the release contains no offer or even a mention of the company's effort to sell securities. Even before this period starts, there can be problems with communications that make any reference to the contemplated offering. In addition, if company executives give interviews where the ultimate date of publication is uncertain, problems can arise. In those cases, the company must take reasonable steps within its control to prevent further distribution of the information during the 30-day period. Perhaps the most famous interview problem arose during the Google IPO. Interviews after the filing of the registration statement also are generally unwise (except as a part of the road show).

The SEC permits the company to continue during this period to publish factual information that is regularly released and intended for use by persons other than in their capacity as investors or potential investors. It discourages any attempt to ramp up publicity in the period prior to the filing. The company should particularly not disclose anything as to valuation or projections of future performance.

From the time that you begin to work on the IPO process, all press releases and interview requests should be cleared with your counsel and your lead underwriter. Your key executives should also meet with company counsel and the lead underwriter to review what may and may not be said publicly about the company.



In addition, companies need to pay particular attention to what information is on their company websites (including any hyperlinked information). The SEC will typically review that and anything there that could relate to the offering could generate questions and cause potential legal issues.

A specific rule (Rule 135) allows you to announce that you are proposing to make a public offering of securities. In a published statement, such as a news release, you must state that the offering will be made only by means of a prospectus. You can provide some limited information, including the amount of securities you propose to sell, the proposed timing of the offering, and a brief explanation of the manner and purpose of the offering.

Once you have filed and the waiting period begins, you are forbidden to make any written offers, such as through sales literature regarding the offering, except by means of the red herring prospectus and a free writing prospectus (described below). Oral selling efforts (conversations between the company or its underwriters and the prospective buyers relating to information in the prospectus) are allowed. But you must be careful even in oral conversations; if they are taped for broadcast or placed on a website, they can be considered a written offer in violation of SEC rules. With the advent of the internet and the improvement in communications technology, the SEC has been forced to adopt rules to set the boundaries between oral and written communications. Written communication is defined to be any communication that is written, printed, a radio or television broadcast, or a graphic communication. Graphic communication includes all forms of electronic media, including audiotapes, videotapes, facsimiles, CD-ROM, electronic mail, internet websites, substantially similar messages widely distributed (rather than

Your purpose is to demonstrate not only the growth potential of your company, but also the executive capacity of your team.

individually distributed) on telephone answering or voice mail systems, computers, computer networks, or other forms of computer data compilation. However, it does not include a communication that, at the time of the communication, originates live, in real-time to a live audience and does not originate in recorded form or otherwise as a graphic communication, although it is transmitted through graphic means. These definitions become very important in dealing with the road show (described below) and information distributed through social networking media. As a part of the briefing that counsel provides to officials in the company, these rules and their application, including to social networking sites, should be reviewed.

To provide companies more flexibility during the offering, in light of modern technology and the wide dispersion of information, companies doing an IPO can now use what are called “free writing prospectuses” during the waiting period after the red herring prospectus (with a price range specified) has been distributed. Free writing prospectuses are any written communication that constitutes an offer to sell the company’s securities after the filing of the registration statement other than the statutory prospectus included in the registration statement or a communication after the effective date of the registration statement that is accompanied or preceded by a statutory prospectus. There are also certain other exceptions, such as the Rule 135 announcement described above. With certain exceptions, free writing prospectuses can also include information on your website, or hyperlinked by you from your website to a third party website.

Free writing prospectuses have to include a prescribed legend and be filed with the SEC. In addition, in an IPO, they can only be distributed to potential investors to whom a red herring has already been delivered. They may contain additional information to that found in the registration statement, but must not conflict with the information found in the registration statement. These new rules are complicated and you should work with counsel to ensure compliance.

Also allowed is a “tombstone” ad: so called because of their formal, sparse wording and lack of adornment. The advertisement may contain only the following limited information: the name of the company, the title of the security, the amount being offered, the offering price, the name of the underwriters, and a notice stating that the ad is not an offer to sell. The purpose of the advertisement is to announce the issue in the press and to tell interested parties about where they can obtain a copy of the prospectus. Companies traditionally issue the tombstone ad after the pricing of the offering. At that time, another news release is usually distributed to announce that the offering has commenced.

The road show

Also common during the quiet period is a two- or three-week speaking tour of the offering company’s top executives and the lead underwriter, often referred to as a road show. The tour often covers a dozen key cities or more where institutional or individual investors have indicated strong interest. In offerings where some shares will be sold internationally, this road show can include international stops.

The road show’s purpose is to enable the executives to meet the prospective underwriters who have been invited into the underwriting syndicate and to make presentations to key potential investors, portfolio managers, and security and industry analysts. These meetings allow people to ask you questions about the company and the material contained in the prospectus. They are meant to build enthusiasm and momentum for the offering and are normally completed within days of the pricing of the offering.

You should view these meetings as opportunities to present the story of your company to those people who will buy your stock, sell the stock for you, or influence the people who buy. The company needs to be extremely cautious prior to presenting forecasts to potential investors and would be wise to discuss the advisability of this with counsel well in advance of the road show.

Many of these key investors, portfolio managers, and analysts will be participating in future quarterly earnings announcement conference calls (after you go public) and otherwise follow the company’s progress. If you are meeting them for the first time, you should take care to convince them that you and your associates are people of ability and integrity who will provide solid leadership for your company in the years ahead. Your purpose is to demonstrate not only the growth potential of your company, but also the executive capacity of your team.

The road show is usually organized by your lead underwriter. The filing requirements of road shows are now covered by an SEC rule (Rule 433 under the 1933 Act). Most road shows will not be deemed to be free writing prospectuses and, therefore, will not need to be filed. Most are live presentations and will be deemed not to be a written communication even if it is simultaneously webcast or transmitted into other locations. The slides that are generally used in the presentations are also not deemed to be a written communication if they are transmitted simultaneously with the presentation. In contrast, prerecorded electronic road shows for an IPO will be deemed a free writing prospectus and will have to be filed, unless the company makes at least one version of the electronic road show available without restriction to any person.

Road shows (like all other publicity during the offering), even if they do not have to be filed with the SEC, are still subject to the antifraud provisions of the securities laws and so you should be very careful about what is said in the road show. The underwriters and your legal counsel will provide coaching on what questions to expect, how to answer them, and what you can and cannot say during those meetings. The road shows are very grueling, but are an important component of the IPO process. Before, after, and between presentations, at breakfast, lunch, and dinner meetings, you may meet with individual analysts who specialize in your industry. The tour can educate the financial community about your company and help generate and sustain interest in your stock through the period of the offering.

Making the best presentation

When you and your top executives present the road show and appear before securities analysts, brokers, and other investors, your company will likely be judged in large measure on the strength of your performance. How clear is the presentation? How well organized is everyone? Can you take the heat of tough questions?

While you can expect guidance and suggestions from your underwriters, attorneys, and others on how to conduct yourselves, you should be sure that you are comfortable with the presentation – both what is in it and how it is presented. This is your opportunity to tell your company's story. And you will have to execute operationally to meet the expectations that you and your management team have set through these presentations and the disclosure in the prospectus.

Choreography. Each member of the executive team should have a specific role in the presentation. It could be that the CEO provides a summary and an introduction to the company and his vision for its future. Other members of the team would provide more detail on marketing, sales, production, and finances.

Visuals. Given today's sophisticated presentation packages and easy-to-produce graphics, audiences expect some visual backup in the form of slides or overheads to support statements about market share and financial performance. While the presentation should not be based entirely on such visuals, they can be used judiciously to make the presentation clear and interesting. Anticipate potential problems and have backup alternatives immediately accessible.

Demonstration. A demonstration of your company's product or service can save a lot of explanation and will emphasize its importance much more compellingly than a verbal description. This is especially true if your product is technologically advanced. If the product is too big or the service is too complex for a demonstration, use photos showing it being used by customers if possible.

Preparation. Rehearse your presentation as much as possible. Each time, executives will discover a weakness or problem that should be corrected. Also practice answering potential questions; use team members (counsel and underwriters) to ask tough questions and then rehearse your answers. Videotaping the rehearsals will facilitate spotting the problem areas. The management team's formal presentation should not last longer than about 30 minutes. You should also allow for 30 minutes or so of questions following the presentation.



Chapter 8. Closing the deal

The closing of a public offering is not a simple affair, governed as it is by both the underwriting industry's traditions...

...and government regulation through the SEC. It is important that everything be done properly so as not to risk wasting the long and costly preparation work and damaging the public perception of your company.

Signing the underwriting agreement

Generally, you do not enter into a written underwriting agreement until after the marketing effort is largely done and the registration is declared effective by the SEC.

Until that time, you have only a draft copy of the underwriting agreement and an oral understanding with the underwriters in some cases, there may be a letter of intent. The purpose of a letter of intent is to outline the basic method of financing acceptable to both parties, the price range in which the underwriters believe the shares can be sold to the public, the approximate expected underwriting compensation, and allocation of expenses. Neither the oral understanding with the underwriters nor the letter of intent is a legal commitment by either side to proceed with any predetermined transaction.

Timing thus becomes quite important as the effective date approaches. The end of the road show and the completion of the book building process (hopefully resulting in significant public momentum for the offering) are targeted to occur at about the same time as the SEC review process is completed. The registration statement is then declared effective. On that day or very shortly thereafter, the lead underwriter and the company agree on the selling price to the public. The lead underwriter and the other underwriters participating in the syndicate also legally agree to their participation in the underwriting.

This agreement among underwriters authorizes the lead underwriter to sign the underwriting agreement, specifies the terms on which the other underwriters will participate in the syndicate, and spells out the responsibilities of the lead underwriter to manage the offering.

Immediately afterward, the underwriting agreement is signed by the company, the lead underwriter, and the selling shareholders, if any. The agreement includes the offering price of the stock; commissions, discounts, and expense allowances; the method of underwriting; and an

indemnification agreement. It also sets a number of conditions to the underwriters' obligation to complete the offering (for example, that there is no material adverse development impacting the company between pricing and closing). Until that time, the company has no legal right to compel the underwriters to proceed with the IPO. Once the underwriting agreement is signed, the company files a Rule 424 final prospectus with the SEC and actual sales pursuant to the offering commence.

As a practical matter, once preparation of the registration statement begins, reputable underwriters rarely refuse to complete the offering unless significant adverse changes in market conditions occur or the registration process reveals serious problems at the company of which the underwriters were previously unaware. The lead underwriter has substantial motives for completing the offering, since it has invested considerable time and expense in investigating the company's business and affairs, helped to prepare the registration statement, and organized a selling syndicate. The public perception of a failed IPO is damaging to the reputations of both the company and the lead underwriter.

Should the market cool significantly during the waiting period, though, it is not unusual for an IPO to be postponed or canceled after the registration process starts. If the market is not willing to accept the originally anticipated price range or to absorb an offering as big as the one contemplated, the company may be faced with the choice of accepting an offering of unsatisfactory size or price, postponing the offering until the market improves, or even abandoning the IPO altogether. If the final size or pricing of the offering is outside the range originally on the distributed red herring, it may be necessary to recirculate a new red herring.

Transfer agents and registrars

For most companies making an IPO, the question of transfer agents and registrars is one of expediency rather than regulation. If your stock is to be traded OTC or listed on the NASDAQ, or the NYSE, you are required to use an independent registrar and transfer agent.

However, a public company will usually have a large number of shareholders, and, as regular trading develops, shares will likely change hands daily. Not only is this an administrative burden, but transfers must be handled with absolute accuracy, because any mistake can lead to claims against the company and possible financial liability.

If your stock is to be traded OTC or listed on the NASDAQ or the NYSE, you are required to use an independent registrar and transfer agent.

Independent agents can assume responsibility for making sure that mistakes in stock transfers do not occur. And, as a practical matter, your agreement with the underwriters may require such independent agents.

You typically should appoint a registrar and a transfer agent before the closing of your IPO. Stock registration and transfer services are provided by commercial banks and trust companies. Companies often appoint the same organization to provide both services.

The transfer agent's primary responsibilities are to handle the transfer of shares from one person to another and to maintain the stock books that are the official records of the names and addresses of the company's owners. Corollary responsibilities assigned to transfer agents may include disbursing cash dividends, mailing annual reports and proxies, distributing stock dividends, and keeping custody of unissued stock certificates.

Registrars are responsible for making sure that stock is not over-issued. They countersign all stock certificates to make sure the number of shares issued is not greater than the number surrendered for cancellation, and they keep active records of all the shares that are outstanding. Registrars keep records of the certificates that have been canceled, lost, or destroyed as well as those that have been issued, so that at any given moment they have an exact record of shares outstanding. Part of their role is to crosscheck the work of the transfer agent.

The lock-up agreement

As part of the closing process, the underwriters will want to make sure that highly visible employees and shareholders of the company do not sell their shares for a period of time after the IPO is completed. This is done both to prevent a bailout but more importantly to allow an orderly trading market to develop without additional shares being dumped into the market. To make sure that this occurs, the underwriters will most likely require that the officers, directors, large shareholders, and other listed management enter into a lock-up agreement. The lock-up agreement is typically 180 days, but can range in its duration from 90 days to one year.

The closing

The closing marks the conclusion of the IPO. In a firm commitment offering, the closing typically occurs within one week after the pricing. This period allows the underwriters to receive payment from purchasers of the stock in the offering. In addition, it provides an opportunity for the company and its underwriters to respond to any significant negative events and, if necessary, withdraw the offering. Such events are very infrequent, but in the case of one company, the IPO was voided and all moneys refunded when its CEO was killed in an automobile accident the evening after going public. In a best efforts offering, the closing will occur after all the shares have been sold or the company and underwriters agree that selling efforts can be concluded.

The closing is a formal meeting to exchange documents, certificates, legal opinions, checks, and receipts and may be attended by the company and its counsel, the lead underwriter and its counsel, the registrars and transfer agent, and the auditors. Among the actual exchanges that occur, the underwriters give the company immediately available funds for the net proceeds of the offering, the registrar and transfer agent give the underwriters the stock certificates, counsel provide their legal opinions on the transaction, and the auditors give the underwriters a second comfort letter as of the closing date, referred to as the bring-down comfort letter. Some of these exchanges occur outside of the actual closing meeting to facilitate the orderly issuance of the shares.



Chapter 9. After you go public

Decisions and technicalities do not come to an end once you have gone public.

Your company's stock price will be affected by rules of both the stock exchanges (or NASDAQ) and the SEC and, very importantly, by the investment community's perception of the company. And, of course, demands will now be made by shareholders.

Trading and aftermarket support

As part of its aftermarket support for your stock, your lead underwriter will normally be the principal market maker. It should stand ready to purchase or sell the stock in the inter-dealer market. Upon the initial sale of your stock, some buyers may purchase shares with the intention of getting in for the initial price rise and then selling. These buyers will sell the same day or several days after acquiring stock at the IPO price, typically called "flipping." Some flipping is good in an IPO, since it provides some additional supply for the aftermarket, but if too much occurs, it could adversely affect the aftermarket, forcing the market price below the IPO price. One of the significant roles of the lead underwriter and the syndicate will be to try and sell securities to investors that are the proper mix of shorter term and longer term holders.

To stabilize the market and prevent or retard a decline in the market price, the lead underwriter, acting on behalf of the syndicate, may enter bids to buy the stock offered by those wishing to sell in the early stages of the IPO. Stabilization is a highly technical practice allowed by the SEC if certain requirements are met. Detailed reports of all stabilizing transactions must be filed with the SEC.

provides flexibility to the underwriters to fine tune the distribution to help create an orderly aftermarket.

Your relationship with the financial community

After you go public, you will want the financial community to continue to take an interest in your company. It is important to develop a good relationship with brokers, analysts, and others, as they play a large role in sustaining market interest in your company's stock.

Investment banking firms and retail brokerage houses maintain investment research departments or groups of analysts who continually study the progress of many companies. In addition, independent analysts follow specific industries and companies within those industries. These people assist investors in evaluating and interpreting the financial affairs of companies. You will meet some of these analysts during your road show, and the familiarity may prove to be helpful.

If analysts develop an interest in your company, they will study your annual and quarterly reports and other information you disclose to the public. They may also conduct management interviews to gather on the spot information, and some of them may visit your company. They will want to meet with top management personnel.

You must take care not to release any material information to someone who may rely on that information to buy or sell stock, unless you simultaneously release it to the general financial community. Concerned with the advantage securities analysts have had over individual investors, the SEC has cracked down on selective disclosure, including to analysts seeking earnings guidance and other non-public information through private discussions with issuers, and enacted Regulation FD in 2000. Regulation FD has changed the way company executives interact with research analysts. Whenever a U.S. public company, or a person acting on the company's behalf, discloses to certain enumerated persons (in general, securities markets professionals and holders of the issuer's securities who may trade on the basis of the information) material nonpublic data and relevant information that may influence investment decisions, Regulation FD requires the company to make public disclosure of that information either simultaneously in the case of intentional disclosure, or promptly, in the case of nonintentional disclosure. So, before starting any discussions with analysts, you should seek advice of counsel and establish a corporate policy regarding disclosures.

Appearances before societies of securities analysts can also be an integral part of your financial public relations program. These people are in a position to recommend to investors the purchase or sale of your stock. If they invite you to make a

After you go public, you will want the financial community to continue to take an interest in your company.

In addition, underwriters are allowed to engage in "over-allotment," whereby they offer and sell more shares than they are obligated to buy under the underwriting agreement. This practice automatically creates a "short" position; that is, they have sold shares they do not have. Their short position is subsequently covered by the stock resold by those speculative buyers, and the offering price is sustained. In addition, the underwriting agreement in a firm commitment offering often gives the underwriters an option to purchase more shares from the company for the purpose of covering over-allotments. (This option is referred to as a green shoe because it was first used in an offering by the Green Shoe Company.) During calendar years 2008 and 2009, almost all IPOs had over-allotment options in their underwriting agreements. A typical over-allotment provision is between ten percent and 15% of the total shares offered in the IPO. This over-allotment option

presentation about the company, take the opportunity to do so, but limit your presentation to information that is already public.

As a public company, you must promptly disclose material information (both positive and negative) to investors, unless (absent certain circumstances) you have a legitimate business purpose for keeping it confidential. You should consult with your counsel for guidance in this area, as the legal requirements are complex and very fact specific. The SEC's Form 8-K current report may be required to be filed currently to disclose this information. See further discussion on Form 8-K requirements in the 1934 Act discussion below.

Public disclosures are generally made through press releases and SEC filings. Because the media reports selectively, you may, on some occasions, want to send the releases directly to shareholders. To make sure that you have satisfied your obligations of full disclosure under Regulation FD, you will want to choose the method that best provides broad, nonexclusionary distribution of information to the public in light of your particular distribution circumstances.

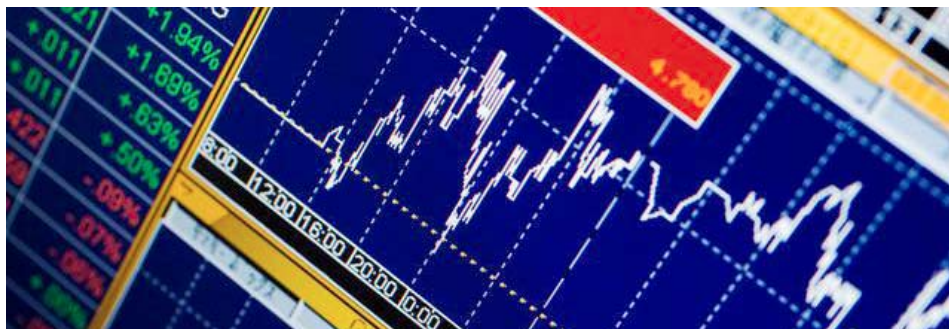
To ensure appropriate, adequate, and timely disclosure, you should consult with counsel to adopt written disclosure policies and procedures that are consistent with Regulation FD. You may want to designate one person in the company to be the investor relations officer, with the responsibilities of (1) responding to requests for information from securities analysts, the trade and business press, and other interested parties and (2) reviewing all proposed press releases and texts or outlines of speeches, or interviews with the press. You should also authorize only certain officers or employees to speak with members of the financial community. You may want to create a disclosure committee. This committee will normally be comprised of members of senior management (including counsel) as well as employees from key parts of your organization. The committee's purpose is to review public disclosures prior to their issuance.

Compliance with securities laws

Once you are a public company, you are subject to a number of federal securities laws. You, your officers, and your directors should meet with counsel to discuss what your obligations and responsibilities are under these laws. We briefly discuss some aspects below; however, you should bear in mind that these laws are extremely complex and that counsel should be involved in making sure that your company complies with them.

Timely disclosure of information

We have discussed above your obligation to disclose material information on a timely basis and not on a selective basis. In many cases, it may be clear that a fact is material. In some cases, it is not. Generally, if you, as an investor, would



consider the fact important in making an investment decision, then it is material information.

Trading on inside information

No one who has material non-public inside information about the company, including those who are merely aware of inside information, should buy or sell the company's stock before that information is released to the public. This applies to all officers, directors, and employees. It also applies to people outside the company who gain access to this information, including family members of officers, directors, and employees of the company; in fact, if an insider tips any other person, both parties may be liable for damages under federal securities laws.

Handling restricted stock

If you or your shareholders are counting on going public to make your stock holdings saleable, you should be aware of restrictions on resale. When an IPO is completed, only the shares sold as a part of the IPO become freely tradable under the 1933 Act. If there was outstanding stock previously issued in private placements, it would be considered "restricted stock" and may be subject to resale restrictions. Restricted stock, and any stock owned by persons who are considered affiliates of the issuer, generally cannot be resold in the public market, unless the stock is included in a registration statement as a new offering or is sold in compliance with Rule 144 of the 1933 Act. Although your shareholders may sell restricted stock without complying with Rule 144, such sales are rare because they fail to take advantage of the safe harbor of Rule 144.

Rule 144 provides, in general, that restricted stock held by non-affiliates can be sold without restriction if it has been held by the person for six months, if the company has been a

No one who has material non-public inside information about the company should buy or sell the company's stock before that information is released to the public.

reporting company under the 1934 Act for at least 90 days and is current in its filings under the 1934 Act; if the company does not meet that test, the holding period is one year. For stock owned by affiliates (and anyone who was an affiliate within the then-previous 90 days), Rule 144 requires the same holding period, but even after that period, imposes volume, manner of sale, and current company public information conditions on sales under Rule 144. These sales can only be made through unsolicited broker transactions or in certain other defined circumstances. In addition, a notice filing is required in certain instances.

Regardless of the Rule 144 provisions, insiders (e.g., officers and directors, shareholders holding more than 10% of the outstanding stock) are often advised to limit their purchase and sale of stock to certain trading windows. These restrictions are discussed below in this [Chapter 9](#).

The 1934 Act

If your stock is listed on a stock exchange, or you have total assets of more than \$10 million and more than 500 shareholders, you must register your class of equity stock under the 1934 Act, unless you otherwise receive an exemption from the SEC prior to having to register. As a part of the IPO process, you typically will file a Form 8-A to have the class of securities being issued in the IPO registered under the 1934 Act. That is a short document that essentially incorporates portions of the 1933 Act registration statement. The 1934 Act subjects your company to certain legal and reporting requirements, some of which are described below.

Periodic reporting requirements. A domestic registrant must file a Form 10-K report annually with the SEC. Form 10-K is designed to provide a continuing update of the disclosures in your registration statement. Consequently, it should contain information about the business, management, the latest audited financial statements, management's certifications regarding the accuracy of the financial statements and the effectiveness of the company's internal controls over financial reporting, and management's discussion and analysis of financial condition and results of operations. Certain disclosures, however, may be somewhat more condensed than those contained in Form S-1. The Form 10-K annual reports for large accelerated filers are due within 60 days after fiscal year end, Form 10-K annual reports for accelerated filers are due within 75 days after fiscal year end, and all other filers must file their annual report within 90 days after fiscal year end. An accelerated filer is defined as an issuer at the end of its fiscal year (1) with public float of at least \$75 million and less than \$700 million as of the last business day of the issuer's most recently completed second fiscal quarter, (2) with at least one annual

report filed under the 1934 Act, (3) that has been subject to the filing requirements of the 1934 Act for at least 12 months, and (4) that is not eligible to file as a smaller reporting company. A large accelerated filer is defined as an issuer at the end of its fiscal year that has a public float of \$700 million or more as of the last business day of the issuer's most recently completed second fiscal quarter, and otherwise satisfies items (2) through (4) in the definition of an accelerated filer. Fewer disclosures and less financial information is required from smaller reporting companies.

Every quarter (other than with respect to the 4th quarter of each year), a domestic registrant must file Form 10-Q. These reports contain quarterly financial statements and certain footnotes which must be reviewed by an auditor prior to the filing of the Form 10-Q and management's certifications regarding the accuracy of the financial statements and the effectiveness of the company's internal controls over financial reporting. These reports will also contain management's discussion and analysis of financial condition and results of operations, and narrative disclosures in the event that specific reportable events (legal proceeding, changes in securities, defaults on senior securities, and, until February 28, 2010, the submission of matters to a vote of security holders) have occurred during the quarter. The Form 10-Q is due within 45 days after quarter-end for a nonaccelerated filer, and smaller reporting company and within 40 days after quarter-end for an accelerated filer or a large accelerated filer.

Form 8-K must be filed within four business days of a reportable event, subject to certain exceptions. The reportable events have been expanded to include the following events: entry into or termination of a material definitive agreement; bankruptcy or receivership; completion of a significant acquisition or disposition; results of operations and financial condition; creation of a direct financial obligation or an obligation under an off-balance sheet arrangement; triggering events that accelerate or increase a direct financial obligation or an obligation under an off-balance sheet arrangement; costs associated with exit or disposal activities; material impairments; notice of delisting or failure to satisfy a continued listing rule or standard; or transfer of listing, unregistered sales of equity securities; material modifications to rights of security holders; effective February 28, 2010, the submission of matters to a vote of security holders; a change in the registrant's auditor; nonreliance on previously issued financial statements or a related audit report or completed interim review; changes in control of the registrant; departure of directors or principal officers; election of directors; appointment of principal officers; amendments to articles of incorporation or by laws; change in fiscal year; temporary suspension of trading under the registrant's employee benefit plans; amendments to the

registrant’s code of ethics; or a waiver of a provision of the code of ethics; Regulation FD disclosure; or other material events. For Form 8-K filings designed to satisfy Regulation FD, “a registrant either furnishing a report on this form under Item 7.01 or electing to file a report on this form under Item 8.01, solely to satisfy its obligations under Regulation FD must furnish such report or make such filing as applicable in accordance with the requirements of Rule 100(a) of Regulation FD.” However, if the Form 8-K is used to disclose material, nonpublic information in accordance with Regulation FD, then the Form 8-K must be filed “simultaneously” for an intentional disclosure and “promptly” for a nonintentional disclosure. Promptly is defined to mean “as soon as reasonably practicable” but no later than 24 hours after the disclosure is learned of and it is both material and nonpublic.

(Note: If you do not need to register under the 1934 Act, you must nevertheless comply with these periodic reporting requirements for the balance of the year in which you went public and for each subsequent year in which you have 500 or more shareholders.)

Section 404 of the Sarbanes-Oxley Act of 2002 requires that the auditor attest to the effectiveness of the internal controls over financial reporting of the company and issue a report in accordance with the PCAOB standards. Section 404 filing requirements are as follows:

Filer	First Section 404(b) reporting requirement
Newly public company (domestic and foreign)	Second annual report
Nonaccelerated filer and smaller reporting company (domestic and foreign)	<p>First fiscal year ending on or after December 15, 2007, but before June 15, 2010 (only need to include management’s report on Internal controls over financial reporting)</p> <p>Fiscal years ending on or after June 15, 2010 (need to include both management’s report on Internal controls over financial reporting and the auditor’s opinion on the effectiveness of Internal controls over financial reporting).</p> <p>There is political activity that may lead to a permanent deferral of the auditor’s attestation report for nonaccelerated filers. At the date of this publication, this deferral had not been finalized. Please consult with your auditor and legal counsel if your company meets this classification.</p>
Domestic company or foreign private issuer that is a large accelerated filer or an accelerated filer	Currently applicable

The Section 404 reports are due at the same time as the related annual report (Form 10-K) in accordance with the above schedule.

XBRL requirements. Domestic and foreign filers that use U.S. GAAP and have a worldwide public company common equity float above \$5 billion as of the end of the second fiscal quarter of their most recently completed fiscal year are now required to file a new exhibit that contains their financial statements in an interactive data format, called eXtensible Business Reporting Language (XBRL). XBRL allows investors and others to pinpoint facts and figures by recognizing the information in the interactive data format through the use of searching software and analytical tools. The filing requirement is being phased in. Other domestic and foreign large accelerated filers using U.S. GAAP must start with fiscal periods ending on or after June 15, 2010. All remaining filers including small reporting companies and foreign private issuers with financial statements prepared in accordance with International Financial Reporting Standards (IFRS) will need to comply for fiscal periods ending on or after June 15, 2011. Subject to this phase-in, new registrants will be required to submit an interactive data file for their first periodic report on Form 10-Q or first annual report on Form 20-F or Form 40-F, if applicable. An XBRL exhibit is not required in an IPO filing.

Proxy statements and annual reports. Before you hold a shareholders’ meeting or seek a written shareholder vote on a matter, you must send out an information statement or, if you are soliciting proxies, a proxy statement. If it is an annual meeting and directors will be elected, you must also send an annual report (often a glossy report updating the shareholders about the company and its activities and financial results for the past year). The SEC dictates the form of the proxy card and the content of the proxy statement (and any other proxy materials), which in some cases must be filed with the SEC 10 days before they are sent or given to shareholders. The SEC also has rules governing the Annual Report.

The Foreign Corrupt Practices Act (FCPA). The FCPA is an amendment to the 1934 Act dealing with certain foreign payments and imposes a statutory requirement for companies to:

- maintain reasonably accurate detailed records of their transactions
- maintain a system of internal accounting control that will be sufficient to reasonably assure that (1) transactions are executed in accordance with management’s authorization, (2) the transactions are recorded properly, (3) access to assets is adequately safeguarded, and (4) there is adequate accountability for the assets

The FCPA was enacted after widespread publicity about “sensitive payments” by companies to government officials, foreign companies and governments, suppliers, customers, and others. Even without the existence of the FCPA, companies (both private and public) would want to maintain adequate records and internal controls. With the FCPA, companies and their employees are subject to legal sanctions for noncompliance.

In addition, the FCPA contains strict prohibitions against bribery of foreign officials in order to obtain or retain business. Foreign officials can include certain individuals in state owned commercial enterprises.

The Sarbanes-Oxley Act. The Sarbanes-Oxley Act’s purpose was to provide reforms for the U.S. financial reporting system to help restore investor confidence. The reforms were significant and included, among others, i) the establishment of the PCAOB, ii) the creation of new rules regarding auditor independence, iii) the creation of new rules regarding audit committee composition, iv) a requirement for CEO and CFO certifications in quarterly and annual reports, v) additional disclosures to be included within the financial statements, vi) a requirement for a code of ethics for senior financial officers, vii) a requirement for a whistleblower policy, viii) the establishment of new monetary as well as criminal penalties, and ix) the acceleration of the filing requirements for annual and quarterly SEC reports. This list does not include all of the reforms instituted by the Sarbanes-Oxley Act. For a more complete discussion of the ramifications of the Sarbanes-Oxley Act as it relates to your company, consult with your legal counsel.

Tender offers. The 1934 Act regulates tender offers and requires disclosure before the commencement of a tender offer. A tender offer is generally made in an effort to gain control of a registrant. As with proxy materials, the goal of disclosing information about tender offers is to ensure that investors are able to make informed noncoerced decisions.

Beneficial ownership reporting. Any person or entity that owns more than 5% of the outstanding shares of a class of stock must file reports pursuant to the 1934 Act. This can be done, depending on the filer’s status and intentions, on a Form 13D or 13G.

Trading activities by insiders. Certain insiders, consisting of shareholders beneficially holding more than 10% of the

stock and all directors and certain officers (defined in Rule 16a-1(f) of the 1934 Act), must file with the SEC reports regarding their stock holdings. An initial report must be filed by the time the company’s 1934 Act registration becomes effective. Any person who subsequently becomes subject to this requirement must file an initial report within 10 days of acquiring that status. Once the initial report is filed, any changes in beneficial holdings (purchase, sale, gift, exercise of options, etc.) must be reported before the end of the second business day following the change. These filing requirements are complex, as are the definitions of beneficial ownership of shares under Section 16 of the 1934 Act, so you will want to be sure that all persons subject to these rules are well informed.

All such reporting persons (except as noted below) are also subject to the short-swing profit provisions of Section 16 of the 1934 Act. If these individuals realize any profits from the purchase and sale or sale and purchase of the company’s stock within a six-month period, they may have to turn over such profits to the company. This can apply whether or not the trading was based on insider information.

Reporting persons are also not permitted to sell securities that they do not own at the time (sell “short”) or, if they do own them, that they do not deliver within 20 days after the sale (sell “short against the box”).

Some companies have “window periods” when they encourage insiders, if they want to buy or sell company stock, to do so. These window periods are typically defined shortly after public announcements of material events, such as earnings releases. These are considered to be periods of time when all material information is public. There are advantages and disadvantages to using these window periods and you should discuss them with counsel before adopting a policy utilizing them.

Regulation BTR (Blackout Trading Restriction) of the SEC, adopted pursuant to Section 306(a) of the Sarbanes-Oxley Act, generally prohibits directors and executive officers from trading activities involving company stock acquired in connection with his or her service or employment as a director or executive officer when participants in company stock and retirement plans (such as a 401(k) plan) are temporarily prohibited from engaging in transactions in such company’s stock in their company stock and retirement plans. This was enacted to deal with the perceived abuses in the Enron situation when company employees were prohibited from selling company stock in their company stock plans, but executives were not prohibited from selling their own company stock.

Any person or entity that owns more than 5% of the outstanding shares of a class of stock must file reports pursuant to the 1934 Act.

Chapter 10. Foreign private issuers

Foreign companies going public in the United States use essentially the same process, but have some special rules that apply to them.

This chapter highlights some special rules for foreign companies considering whether to go public in the United States and should be read in conjunction with the remaining chapters which further describe that process.

Most foreign companies who conduct IPOs in the United States are called “foreign private issuers” under the federal securities laws. A foreign private issuer is defined as an issuer that is incorporated or organized under the laws of a foreign country, except an issuer meeting the following conditions: (1) more than 50% of the issuer’s outstanding voting securities are directly or indirectly held by residents of the U.S. and (2) any of the following: (a) the majority of the executive officers and directors are U.S. citizens or residents, (b) more than 50% of the assets of the issuer are located in the U.S., or (c) the business of the issuer is administered principally in the U.S. This test is required to be performed annually, as of the last business day of the issuer’s most recently completed second fiscal quarter. A foreign issuer (other than a foreign government) that does not meet the definition of a foreign private issuer must use the same registration and reporting forms as a domestic issuer. A foreign private issuer may also voluntarily elect to use the registration and reporting forms that domestic issuers use.

The marketing process for a U.S. IPO of a foreign private issuer is generally very similar to that described for a domestic issuer. The team members are the same, the prepublic planning process is the same and there is a SEC filing process just as there is with domestic U.S. companies. These processes, however, can take more time because of the added complexities of being a foreign private issuer. This can be particularly true with the accounting and due diligence portions of the work. In addition, the same rules govern public communications before, during, and after the IPO.

Many foreign private issuers who publicly offer securities in the U.S. do so using American Depositary Receipts (ADRs). ADRs are issued by a depository institution in the U.S. (which has contracted with the foreign issuer to provide this service) and represent a specified amount of equity securities of the foreign issuer. If you were doing an IPO, you would deposit your equity shares with the depository which would then issue ADRs to the U.S. investors purchasing securities in the IPO. ADRs are meant to mirror the underlying equity securities (though there can be important differences which should be discussed with counsel) and are used to facilitate the clearance of transactions on U.S. markets. ADRs are also priced in U.S. dollars.



French Franc	308000	8180
British Pound	87864	4799
Dutch Guilder	4799	26500
Belgian Franc	25000	1163
Danish Krone	1163	245855
Peseta	245855	568
Irish Punt	568	965
Greek Dracma	965	145900
Portuguese Escudo	138000	1799

Set forth below are short summaries of some key differences in the IPO process for foreign private issuers. The following is a brief summary only and does not describe all of the differences in disclosure and the application of the securities laws between foreign and domestic issuers. You should consult with your advisors before moving forward on the IPO process.

1933 Act filing and disclosure differences

Form F-1 (and not Form S-1) is used by foreign private issuers to register with the SEC. Form F-1 takes most of its disclosure requirements from those found in Form 20-F. Form F-1 provides certain financial statement and disclosure accommodations from that found in Form S-1. While these accommodations can be made, often the underwriters will try to make most parts of the prospectus (other than the compensation disclosure) for a foreign private issuer look similar (substantively) to a prospectus for a domestic issuer.

In addition, the SEC considers ADRs to be separate securities from the issuer’s underlying equity securities and so a Form F-6 is required to be filed by the depository bank with the SEC.

Certain accommodations are available for a foreign private issuer in the Selected Financial Data section of the registration statement. For example, if the foreign private issuer is unable to provide information for the earliest two years of the five-year period without unreasonable effort or expense, those periods may be omitted. However, the investment bankers may request that a foreign private issuer provide all five years of Selected Financial Data. In Selected Financial Data, a foreign private issuer is required to disclose, at least, net sales or operating revenues, income (loss) from operations and continuing operations and net income (loss), in total and per share amounts; total assets; net assets; capital stock; number of shares as adjusted to reflect changes in capital; and dividends declared per share in both the currency of the financial statements and the host country currency, including the formula used for any adjustments to dividends

declared. Selected Financial Data should be presented in the same currency as the financial statements.

A foreign private issuer must include a statement of capitalization and indebtedness in the Form F-1 registration statement. While the form requires that this be dated no earlier than 60 days before the date of the prospectus, in practice many companies use data as of the same date as the most recent balance sheet presented in the registration statement, with an “as adjusted” column disclosing any significant changes.

The MD&A found in a Form S-1 can be titled the “Operating and Financial Review and Prospects” in the Form F-1; however, substantively, it is very similar to the MD&A in domestic issuer offerings.

Differences between a domestic issuer and a foreign private issuer in compensation disclosures are perhaps the area of most interest to executives. Foreign private issuers are permitted to provide aggregate data only (if that is what is provided in the issuer’s home country) and much less information concerning individual executive compensation. This was done in part to accommodate disclosure to that of the home market and to respond to the legitimate safety concerns of foreign executives if their individual compensation became publicly known.

Foreign private issuers must also disclose the effect of any laws, decrees, regulations, or other legislation of the home country of the issuer that may affect the import or export of capital, including the availability of cash for use by the parent company or the remittance of dividends, interest or other payments to non-resident security holders. Any tax consequences that can affect non-resident security holders must also be disclosed.

Foreign private issuers can make their initial Form F-1 filing on a non-public basis in order to allow the SEC and the foreign private issuer to work out any difficult disclosure issues confidentially. On occasion, these issues have to do with the inconsistencies in disclosure regimes between the foreign jurisdiction and the U.S. If those issues cannot be worked out, the attempted filing is never public and so the foreign company’s reputation is not damaged by the failed attempt to register their stock in the U.S. If the foreign company wants to distribute its red herring and conduct a road show, it will have to publicly file a registration statement.

Audit requirements

A foreign private issuer is generally required to include audited balance sheets as of the end of the two most recent fiscal years, and audited statements of operations, cash flows, changes in shareholders’ equity, and comprehensive income for the three most recent fiscal years. Such financial statements may be presented in accordance with either U.S. GAAP, IFRS as issued by the IASB, or local accounting principles. Eligible foreign private issuers reporting in U.S. GAAP or IFRS as issued by the IASB that meet certain criteria may be eligible to present only two years of audited statements of operations, cash flows, changes in shareholders’ equity, and comprehensive income, instead of three. If the foreign private issuer presents its financial statements in accordance with local accounting principles, it must quantify and reconcile material differences to U.S. GAAP and provide all other information required by U.S. GAAP and Regulation S-X. However, first-time foreign private issuer registrants that present their financial statements in accordance with local accounting principles, are only required to provide reconciliations of the financial statements and selected financial data to U.S. GAAP for the two most recently completed fiscal years and any interim period required in the registration statement. While reconciliations to U.S. GAAP initially are required only for two years, the registrant’s financial statements still need to be presented in the registration statement for all of the periods noted above.

Unaudited interim financial statements covering at least first six months of the fiscal year, as well as the comparable period in the prior year will be required when the Form F-1 registration statement is dated more than nine months after the end of the last audited financial year. In practice, however, the investment bankers may impose on a foreign private issuer the domestic requirements as to the age of the financial statements in an IPO.

The XBRL rules applicable to foreign private issuers are set forth in [Chapter 4](#) under Audit Requirements.

Corporate governance differences

The requirements governing the composition of the board of directors and the audit committee can be different for foreign private issuers. Foreign private issuers are exempt from the audit committee independence rules and can have members of the audit committee who are not independent, such as, a non-management employee representative, a non-management affiliated person who only has observer status, or a non-management governmental representative. In addition, the foreign private issuer is exempt from the audit committee independence rules if the foreign private

issuer has a board of statutory auditors (or similar body), or has statutory auditors, established and selected pursuant to home country legal or listing provisions requiring or permitting such a board or body and that board or body complies with additional SEC standards that are meant to assure that board or body or statutory auditors are independent of management. The SEC also has a provision under its independence rules recognizing that where, as in some foreign countries, companies have two-tiered boards, the “board of directors” means the supervisory or non-management board.

Both the NYSE and NASDAQ also permit foreign private issuers generally to follow home country rules rather than their rules. However, both specify certain exceptions to these accommodations. The NYSE requires that all foreign private issuers meet the SEC requirements for audit committees and notify the exchange of non-compliance with exchange corporate governance rules. The foreign private issuer must also disclose differences between home country and NYSE rules. NASDAQ specifies that (i) foreign private issuers must meet the SEC requirements for audit committees; (ii) foreign private issuers are not exempt from the requirement to make a public announcement if its audit report contains a “going concern” qualification; and (iii) foreign private issuers must notify it in the event of any material non-compliance with NASDAQ corporate governance rules.

After the IPO – 1934 Act filings

Periodic filings. A foreign private issuer is required to file a Form 20-F annual report annually with the SEC within six months after the fiscal year end. Effective for fiscal years ending on or after December 15, 2011, annual filings on Form 20-F will be due four months after an issuer’s fiscal year end. A Form 20-F is similar to a Form 10-K and extends certain accommodations to foreign private issuers. However, similar to domestic issuers, annual reports on Form 20-F must contain the officer certifications required by the Sarbanes-Oxley Act.

A foreign private issuer is exempt from the Form 10-Q quarterly reporting and Form 8-K current reporting requirements. Rather, a foreign private issuer is required to furnish promptly (after the material contained in the report is made public) on Form 6-K material information which the issuer (1) files or is required to file with a foreign stock exchange, if made public by that exchange; (2) makes or is required to make public by its domestic laws; or (3) distributes or is required to distribute to its securities holders. Failure to make these filings could mean that the foreign private issuer is not permitted by the SEC to use the

shorter form of 1933 Act registration statement in future filings (if otherwise allowed to do so).

Corporate governance: Foreign private issuers with securities listed on a national securities exchange are required to provide a concise summary in their annual reports of any significant ways in which its corporate governance practices differ from those followed by domestic companies under the listing standards of that exchange.

Proxy rules. Foreign private issuers are exempt from the proxy rules under 1934 Act Rule 3a12-3(b). Reporting of Trading Activities by Insiders. Foreign private issuers and their officers and directors are largely exempt from the insider reporting and short-swing trading provisions of Section 16 of the 1934 Act.

Regulation FD. Regulation FD specifically exempts foreign private issuers from its provisions. However, many foreign private issuers still comply with the regulation, in part because they can still be liable for selective disclosures under other theories of liability.

Foreign Corrupt Practices Act. Foreign private issuers are subject to both the books and records provisions and the antibribery provisions of the FCPA, just as are domestic companies. This can be a surprise to foreign companies and a number have been prosecuted under the FCPA.

Sarbanes-Oxley Act. Foreign private issuers that are reporting companies under the 1934 Act are subject to the provisions of the Sarbanes-Oxley Act, though there are some accommodations made for foreign private issuers. These accommodations include the areas of audit committee independence (see above), periods in which trading is prohibited under company stock and retirement plans (SEC Regulation BTR), and the use of non-GAAP financial measures (SEC Regulation G). Foreign private issuers conducting an IPO are not required to immediately comply with the independent auditor attestation of the effectiveness of the internal controls over financial reporting under Section 404 of Sarbanes-Oxley. See the chart in [Chapter 9](#) on this subject for the implementation schedule for such attestations. Foreign private issuers should pay particular attention to the requirements of Sarbanes-Oxley before they decide to proceed with an IPO in the U.S.

Appendix A:

The U.S. Securities and Exchange Commission

In the chaotic securities markets of the 1920s, companies often sold stocks and bonds on the basis of promises of fantastic profits without disclosing any meaningful information to investors. These conditions contributed to the disastrous stock market crash of 1929. In response, the U.S. Congress enacted the federal securities laws and created the SEC to administer them.

The SEC is an independent regulatory agency with responsibility for administering the federal securities laws. The purpose of these laws is to protect investors in securities markets that operate fairly and to ensure that investors have access to all material information concerning publicly traded securities. The Commission also regulates firms engaged in the purchase or sale of securities, people who provide investment advice, and investment companies.

Five Commissioners sit on the SEC, with one designated as Chairman by the President of the United States. All Commission members are appointed by the President, with the advice and consent of the Senate, for fixed five-year terms. The Commission is headquartered in Washington, D.C., and operates regional offices in 11 cities. The principal divisions and offices of the Commission are:

Division of Corporation Finance

Corporation Finance has the overall responsibility of helping the commission oversee public disclosure of important information. Its work includes reviewing registration statements and periodic reports (10-Ks, 10-Qs, and 8-Ks), as well as documents concerning tender offers, proxy solicitations, and merger and acquisitions.

Division of Trading and Markets

Trading and Markets establishes and maintains standards for fair, orderly, and efficient markets. This includes the registration and regulation of broker-dealers and the oversight of self-regulatory organizations (including the stock exchanges) and other participants (such as transfer agents). The division also oversees the Securities Investor Protection Corporation and the Municipal Securities Rulemaking Board.

Division of Investment Management

Investment Management ensures compliance with regulations regarding the registration, financial responsibility, sales practices, and advertising of investment companies and of investment advisors. Staff in this division also review new products offered by these entities. The division reviews and processes investment company registration statements, proxy statements, and periodic reports under the 1933 Act.

Division of Risk Strategy and Financial Innovation

Risk Strategy and Financial Innovation was created on September 16, 2009, to assist the Commission in the identification of developing risks and trends in the financial market. The division combines the Office of Economic Analysis (OEA), the Office of Risk Assessment (ORA), and other functions. The division will perform all of the functions previously performed by OEA and ORA, along with the following: (1) strategic and long-term analysis; (2) identifying new developments and trends in financial markets and systemic risk; (3) making recommendations as to how these new developments and trends affect the Commission's regulatory activities; (4) conducting research and analysis in furtherance and support of the functions of the Commission and its divisions and offices; and (5) providing training on new developments and trends and other matters.

Division of Enforcement

Enforcement is charged with enforcing federal securities laws. Enforcement responsibilities include investigating possible violations of the federal securities laws and recommending appropriate remedies for consideration by the Commission.

Office of International Affairs

The Office of International Affairs promotes investor protection and cross-border securities transactions by advancing international regulatory and enforcement cooperation, promoting the adoption of high regulatory standards worldwide, and formulating technical assistance programs to strengthen the regulatory infrastructure in global securities markets. The office works with a global network of securities regulators and law enforcement authorities. The office often becomes involved with offerings of international companies.

Office of the Chief Accountant

The Office of the Chief Accountant is the principal advisor to the Commission on accounting, financial reporting, and auditing matters. The Office of the Chief Accountant also works closely with domestic and international private-sector accounting and auditing standards-setting bodies (e.g., the Financial Accounting Standards Board, the International Accounting Standards Board, and the PCAOB), consults with registrants, auditors, and other Commission staff regarding the application of accounting standards and financial disclosure requirements, and assists in addressing problems that may warrant enforcement actions.

Office of Interactive Disclosure

The office of interactive disclosure carries out the Commission's commitment to make the financial disclosure accessible and easy to use through the application of interactive data.

For more information on the SEC, visit their website at www.sec.gov.

Appendix B:

Registration exemptions

Registration requirements apply to securities of both U.S. and foreign companies or governments sold in the U.S. A company's securities may qualify for one of several exemptions from the registration requirements. The following exemptions under the federal securities laws are the most common ones. You must also comply with all applicable state securities law registration requirements, or find exemptions under state law.

It is also important to note that whether or not securities are registered, the antifraud provisions under the federal and applicable state securities laws apply to all sales of securities. These descriptions of the exemptions are summaries only and the company should consult with its legal counsel prior to attempting any issuance of securities.

Private offering exemption

Section 4(2) of the 1933 Act exempts from registration "transactions by an issuer not involving any public offering." To qualify for this exemption, the purchasers of the securities must:

- have enough knowledge and experience in finance and business matters to evaluate the risks and merits of the investment (the "sophisticated investor"), or be able to bear the investment's economic risk;
- have access to the type of information normally provided in a prospectus; and
- agree not to resell or distribute the securities to the public.

In addition, public solicitation or general advertising in connection with the offering is prohibited.

The precise limits of this private offering exemption are uncertain as they have generally been created pursuant to old SEC interpretations and fact-specific court decisions. As the number of purchasers increases and their relationship to the company and its management becomes more remote, it is more difficult to show that the transaction qualifies for the exemption. If securities are offered to even one person who does not meet the necessary conditions, the entire offering may be in violation of the 1933 Act.

The SEC has adopted a "safe harbor" rule under Section 4(2) of the 1933 Act. That is Rule 506, which is part of Regulation D and is described below. Rule 506 provides objective standards that may be relied on to meet the requirements of the Section 4(2) exemption.

Regulation D of the 1933 Act

Regulation D establishes three exemptions from 1933 Act registration.

Rule 504

Rule 504 provides an exemption for the offer and sale by a private company of up to \$1 million of securities in a 12-month period. Some of the most important characteristics of a Rule 504 offering are:

- You can sell securities to an unlimited number of persons;
- You may not make a general solicitation or advertising to market the securities; and
- Purchasers receive securities that are "restricted." This means that they may not sell their securities in the open market without registration or other sales limits imposed on privately placed securities.

Rule 504 does however allow offerings where a general solicitation or advertising is allowed and where purchasers do receive unrestricted stock in certain circumstances where state securities laws provide for investor protections or where only accredited investors (as defined below) purchase the securities.

Rule 504 does not require issuers to give disclosure documents to investors. Nonetheless, sufficient information should be provided to investors to avoid violating the antifraud provisions of the securities laws.

Rule 505

Rule 505 provides an exemption for offers and sales of securities totaling up to \$5 million in any 12-month period. Under this exemption, you may sell to an unlimited number of "accredited investors" (defined below) and up to 35 other persons (who do not need to satisfy the sophistication or wealth standards associated with other exemptions). The issued securities are "restricted," and investors may not resell them for at least a year without registering the transaction. General solicitations and advertising is not allowed. There are also required disclosures to nonaccredited investors and certain other requirements. This exemption is rarely used.

Rule 506

Rule 506 is a "safe harbor" for the private offering exemption. If your company satisfies the following standards, you can be assured that you are within the federal exemption and can raise an unlimited amount of capital:

- You cannot use general solicitation or advertising to market the securities

- You can sell securities to an unlimited number of accredited investors and up to 35 other purchasers. Unlike Rule 505, all nonaccredited investors (either alone or with a purchaser representative) must be sophisticated
- It is up to you to decide what information you give to accredited investors, so long as it does not violate the antifraud prohibitions. Nonaccredited investors must be given disclosure documents that generally are the same as those used in registered offerings
- You must be available to answer questions by prospective purchasers

Purchasers receive “restricted” securities. Consequently, purchasers may not freely trade the securities in the secondary market after the offering.

An accredited investor is defined as:

- a bank, insurance company, registered investment company, business development company, or small business investment company
- an employee benefit plan (within the meaning of the Employee Retirement Income Security Act) if a bank, insurance company, or registered investment advisor makes the investment decisions, or if the plan has total assets in excess of \$5 million
- a charitable organization, corporation, or partnership with assets exceeding \$5 million
- a director, executive officer, or general partner of the company selling the securities
- a business in which all the equity owners are accredited investors
- a natural person with a net worth of at least \$1 million
- 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 trust with assets of at least \$5 million, not formed to acquire the securities offered, and whose purchases are directed by a sophisticated person (has sufficient knowledge and experience in financial and business matters to make the person capable of evaluating the merits and risks of the prospective investment)

California limited offering exemption - Rule 1001

SEC Rule 1001 provides an exemption from the registration requirements of the 1933 Act for offers and sales of securities, in amounts of up to \$5 million, that satisfy the conditions of §25102(n) of the California Corporations Code. This California law exempts from California securities law registration offerings made by California companies to “qualified purchasers whose characteristics are similar to, but not the same as, accredited investors under Regulation D. The exemption is also available to non-California

businesses that can attribute more than 50% of property, payroll, and sales to California and if more than 50% of outstanding voting securities of the issuer are held by persons having addresses in California. This exemption allows some limited methods of general solicitation prior to sales.

Exemption for sales of securities through employee benefit plans - Rule 701

The SEC’s Rule 701 exempts sales of securities if made to compensate employees. This exemption is available only to companies that are not subject to 1934 Act reporting requirements. You can sell at most the greater of \$1,000,000, 15% of the total assets of the company, or 15% of the outstanding amount of the class of securities being offered. If you sell more than \$5 million in securities in a 12-month period, you need to provide limited disclosure documents to your employees. Employees receive “restricted securities” in these transactions and may not freely offer or sell them to the public. The offers and sales under this exemption are part of a single, discrete offering and are not subject to integration with any other offers or sales.

Rule 144A of the 1933 Act

Rule 144A provides a “safe harbor” from registration for sales by persons other than issuers or dealers who sell securities in compliance with four conditions:

- Securities may be sold only to types of entities that may be characterized as qualified institutional buyers or “QIB”
- The seller must take reasonable steps to ensure that the purchaser is aware that the seller may rely on the Rule 144A exemption
- The securities must not, at the time of issuance, be of the same class of securities listed on a national securities exchange or quoted on the NASDAQ; and
- When the securities sold are of an issuer that is neither a 1934 Act reporting company nor a company exempt from reporting pursuant to Rule 12g3- 2(b), the holder of the securities and any prospective purchaser have the right to obtain certain specified, reasonably current information from the issuers.

Rule 144A does not apply to sales by the issuer of the securities (the company). However, because sales pursuant to Rule 144A are deemed not to be a distribution of securities, it allows issuers to make private placements of securities to QIBs, who can then resell such securities under Rule 144A. A market for Rule 144A securities has developed among sophisticated institutional investors.

Appendix C: The Securities Exchanges

Securities are bought and sold in a number of different markets. The best known are the NYSE and the NYSE Amex Equities (formerly known as the American Stock Exchange), both located in New York City. In addition, six regional exchanges are located in cities throughout the country. Many securities are not traded on a floor exchange, but are said to be traded OTC through a large network of securities brokers and dealers. In the NASDAQ, trading in OTC stocks is accomplished through on-line computer listings of bid and asked prices and completed transactions.

Corporate securities may be traded on an exchange only after the issuing company has applied and met the exchange's listing standards; these may include requirements as to the company's assets, number of shares publicly held, and the number of shareholders. NASDAQ is also a SEC registered exchange (though, in contrast to the NYSE, it is essentially an electronic exchange) and has certain listing standards that must be met before securities may be traded in that market. All the markets apply different standards to initial listings than they do for continued listings. Listing standards are updated frequently, and you can obtain the current parameters for inclusion at the following websites: www.nasdaq.com and www.nyse.com. The requirements for initial listings of domestic corporations on the NASDAQ and the NYSE are outlined in the following tables.

NASDAQ global select market initial listing requirements

Companies must meet all of the criteria under at least one of the three standards below.

Requirements	Standard 1	Standard 2	Standard 3
Pretax earnings ¹ (income from continuing operations before income taxes)	Aggregate in prior three fiscal years ≥ \$11 million and Each of the two most recent fiscal years ≥ \$2.2 million and Each of the prior three fiscal years ≥ \$0	N/A	N/A
Cash flows ²	N/A	Aggregate in prior three fiscal years ≥ \$27.5 million and Each of the prior three fiscal years ≥ \$0	N/A
Market capitalization	N/A	Average ≥ \$550 million over prior 12 months	Average ≥ \$850 million over prior 12 months
Revenue	N/A	Previous fiscal year ≥ \$110 million	Previous fiscal year ≥ \$90 million
Bid price	\$4	\$4	\$4
Market makers ³	3 or 4	3 or 4	3 or 4
Corporate governance ⁴	Yes	Yes	Yes
Round lot shareholders	450	450	450
or	or	or	or
Total shareholders ⁵	2200	2200	2200
Publicly held shares ⁶	1,250,000	1,250,000	1,250,000
Market value of publicly held shares	\$ 70 million	\$ 70 million	\$ 70 million

¹ In calculating income from continuing operations before income taxes for purposes of Rule 5315(i)(3)(A), NASDAQ will rely on a company's annual financial information as filed with the Securities and Exchange Commission (SEC) in the company's most recent periodic report and/or registration statement. If a company does not have three years of publicly reported financial data, it may qualify under Rule 5315(f)(3)(A) if it has (i) reported aggregate income from continuing operations before income taxes of at least \$11 million and (ii) positive income from continuing operations before income taxes in each of the reported fiscal years. A period of less than three months shall not be considered a fiscal year, even if reported as a stub period in the company's publicly reported financial statements.

² In calculating cash flows for purposes of Rule 5315(i)(3)(B), NASDAQ will rely on the net cash provided by operating activities reported in the statements of cash flows, as filed with the SEC in the company's most recent periodic report and/or registration statement, excluding changes in working capital or in operating assets and liabilities. A period of less than three months shall not be considered a fiscal year, even if reported as a stub period in the company's publicly reported financial statements.

³ A company that also satisfies the requirements of an electronic communications network (ECN) is not considered a market maker for the purpose of these rules. Rule 5405(6) or 5405(6) (2) is required to have three market makers. Otherwise, the company is required to have four market makers.

⁴ See "Corporate governance" in Chapter 4.

⁵ Round lot and total shareholders include both beneficial holders and holders of record.

⁶ Publicly held shares is defined as total shares outstanding, less any shares held directly or indirectly by officers, directors or any person who is the beneficial owner of more than 10% of the total shares outstanding of the company.

NASDAQ global market listing requirements

Companies must meet all of the criteria under at least one of the four standards below.

	Standard 1	Standard 2	Standard 3	Standard 4
Shareholders' equity	\$15 million	\$30 million	N/A	N/A
Market value of listed securities ¹ ,	N/A	N/A	\$75 million	N/A
Total assets and	N/A	N/A	N/A	\$75 million and
Total revenue (in latest fiscal year or 2 of last 3 fiscal years)	N/A	N/A	N/A	\$75 million
Income from continuing operations before income taxes (in latest fiscal year or 2 of last 3 fiscal years)	\$1 million	N/A	N/A	N/A
Publicly held shares ²	1.1 million	1.1 million	1.1 million	1.1 million
Operating history	N/A	2 years	N/A	N/A
Market value of publicly held shares	\$8 million	\$18 million	\$20 million	\$20 million
Bid price	\$4	\$4	\$4	\$4
Shareholders (round lot holders) ³	400	400	400	400
Market makers	3	3	4	4
Corporate governance ⁴	Yes	Yes	Yes	Yes

¹ The term, "listed securities", is defined as "securities listed on NASDAQ or another National Securities Exchange."

² Publicly held shares is defined as the total shares outstanding, less any shares held directly or indirectly by any officers, directors, or any other person who is the beneficial owner of more than 10% of the total shares outstanding of the company.

³ Round lot holders are shareholders of 100 shares or more. The number of beneficial holder is considered in addition to holders of record.

⁴ See "Corporate governance" in Chapter 4.

NASDAQ Capital market

Companies must meet all of the criteria under at least one of the three standards below.

	Standard 1	Standard 2	Standard 3
Shareholders' equity	\$5 million	\$4 million	\$4 million
Market value of publicly held shares	\$15 million	\$15 million	\$5 million
Operating history	2 years	N/A	N/A
Market value of listed securities ¹	N/A	\$50 million	N/A
Net income from continuing operations (in the latest fiscal year or in 2 of the last 3 fiscal years)	N/A	N/A	\$750,000
Publicly held shares ²	1 million	1 million	1 million
Bid price	\$4	\$4	\$4
Shareholders (round lot holders) ³	300	300	300
Market makers	3	3	3
Corporate governance	Yes	Yes	Yes

¹ The term, "listed securities", is defined as "securities listed on NASDAQ or another National Securities Exchange."

² Publicly held shares is defined as the total shares outstanding less any shares held directly or indirectly by officers, directors, or any other person who is the beneficial owner of more than 10% of the total shares outstanding of the company. In the case of ADRs at least 400,000 shall be issued.

³ Round lot holders are considered holders of 100 shares or more. The number of beneficial holders is considered in addition to holders of record.

NYSE Amex Equities (formerly known as American Stock Exchange) listing requirements

Companies must meet all of the criteria under at least one of the four standards below.

	Standard 1	Standard 2	Standard 3	Standard 4
Pretax income from continuing operations (in last fiscal year or 2 of last 3 fiscal years)	\$750,000	N/A	N/A	N/A
Market capitalization	N/A	N/A	\$50 million	\$75 million, OR at least \$75 million in total assets and \$75 million in revenues
Market value of public float	\$3 million	\$15 million	\$15 million	\$20 million
Minimum market price	\$3	\$3	\$2	\$3
Operating history	N/A	2 years	N/A	N/A
Shareholders' equity	\$4 million	\$4 million	\$4 million	N/A
Corporate governance	Yes	Yes	Yes	Yes
Public shareholders/public float (shares) ¹	Option 1: 800/500,000 Option 2: 400/1,000,000 Option 3: 400/500,000 ²			

¹ Public shareholders and public float do not include shareholders or shares held directly or indirectly by any officer, director, controlling shareholder or other concentrated (i.e. 10% or greater), affiliated, or family holdings.

² Option 3 requires a daily trading volume of 2,000 shares during the six months prior to listing.

NYSE listing requirements

U.S. companies must meet the minimum distribution criteria and one of the four financial criteria, earnings, cash flow, pure valuation, or assets and equity, under the U.S. standards.

For Non-U.S. companies, the NYSE offers two sets of standards – domestic and worldwide – under which companies may qualify for listing. A company must satisfy both the distribution criteria and financial criteria (earnings and either cash flow or pure valuation) within that particular standard.

Distribution criteria	U.S. standards	Non-U.S. standards	
		Domestic	Worldwide
Round lot holders or	400	400 (U.S.)	5,000
Total shareholders ...together with	N/A	2,200	N/A
Average monthly trading volume (for the most recent six months) or	N/A	100,000 shares	N/A
Total shareholders ...together with	N/A	500	N/A
Average monthly trading volume (for the most recent 12 months)	N/A	1,000,000 shares	N/A
Public shares outstanding ¹	1,100,000	1,100,000	2,500,000
Market value of public shares ¹ IPOs, spin-offs, carve-outs, and affiliated companies	\$ 40 million	\$ 40 million	\$ 100 million
Minimum bid price	\$ 4	\$ 4	\$ 4
Earnings			
Aggregate pretax earnings for the last three years and	10 million	10 million	100 million
Minimum in each of the two preceding year pretax earnings, or	2 million ²	2 million ²	25 million
Aggregate pretax earnings for the last three years and	12 million	12 million	N/A
Minimum in the most recent year and	5 million	5 million	N/A
Minimum in the next most recent year and	2 million	2 million	N/A
Cash flow			
For companies with not less than \$500 million ¹ in global market capitalization and \$100 million in revenues in the most recent 12 months: Aggregate for the last three years operating cash flow (each year must report a positive amount for Domestic) and	25 million	25 million	100 million
Minimum cash flow in each of 2 preceding years or	N/A	N/A	25 million
Pure valuation			
Revenues for the most recent fiscal year and	75 million	75 million	75 million
Global market capitalization ¹	750 million	750 million	750 million
Asset and equity			
Global market capitalization ¹	150 million	N/A	N/A
Total Assets	75 million	N/A	N/A
Shareholders' equity	50 million	N/A	N/A

¹ In connection with IPOs, the NYSE will accept assurance from the company's underwriter that the offering will meet or exceed the exchange standards.

² Third year must be positive.

³ Earnings for all three years must be positive.

⁴ For new entities with a parent or affiliated company listed on the NYSE, the global market capitalization requirement is 500 million if the affiliated company has at least 12 months of operating history, the affiliated listing company is in good standing, and the affiliated listed company retains control of the entity.

Appendix D:

A timetable for going public

A projected timetable for an IPO of ABC Company is offered below. In this example, ABC's fiscal year end is December 31. Audited financial statements are available for each year that ABC has been in existence, and the auditors are in the process of completing the current year's audit. It should be noted that this is only an example of an IPO timetable. There are many variables that can either cause the timing to be accelerated or delayed. As an example, the expected period for the SEC to respond with their initial comments on the company's first registration statement is approximately 30 days. While this is the time period that the SEC aspires to, the time period to receive comments may be longer.

The many documents and procedures listed in the timetable are explained in Chapters 6 through 8. Abbreviations are as follows: ABC, company; CC, company counsel; A, auditors; U, underwriters; and UC, underwriters' counsel.

ABC Company: Schedule of events and responsibilities

Summary of key dates	Dates	Days
Organizational meeting and due diligence	December 15	1
First draft of S-1 distributed without financial statements	December 27	13
Due diligence/first drafting session	January 6	23
Second drafting session	January 14	31
Third drafting session	January 21-22	45
Final drafting session at printers	February 4-5	52-53
Target filing date with audited financial statements where other parts of prospectus are prepared well in advance	February 5	53
Expected receipt of first round of SEC comments	March 7-8	83-84
Drafting session	March 9-10	85-86
Public offering effective	April 17	124
Closing	April 23	130

Detailed schedule		
Date	Activity	Responsibility
Prior to December 1	Board of Directors meeting(s) to discuss IPO and ultimately to authorize preparation of registration statement and engagement of the lead underwriter	ABC, CC
December 15	Initial organization meeting and due diligence: Review timetable Review letter of intent and discuss underwriting issues Discuss underwriters' fees and compensation Assign registration statement preparation responsibilities Identify accounting and other issues Provide customer contracts Select printer Review financial forecasts Management due diligence presentations Discuss transfer agent and registrar Prepare list of parties involved (phone numbers, addresses, secretaries, etc.) referred to as the working group list	All
December 27	First draft of registration statement distributed	ABC, CC
January 6	First drafting session and due diligence: Complete due diligence presentations Review draft of registration statement Discuss obstacles	All
January 6-10	Revise registration statement; underwriters' counsel to draft and distribute underwriters' agreement	All
January 11	Distribution of second draft of registration statement	ABC, CC
January 14-15	Second drafting session to review registration statement	All
January 15-31	Questionnaires completed by officers, directors, and 10% shareholders, and returned to company counsel for review	ABC, CC
January 18	Distribution of third draft of registration statement	ABC, CC

Detailed schedule		
Date	Activity	Responsibility
January 18	Distribution of draft of management's discussion and analysis of financial position and results of operations	ABC, CC, A
January 21–22	Third drafting session to review registration statement	All
January 23	Company counsel and underwriters' counsel meet to discuss Blue Sky problems and underwriting documents	CC, UC
January 28	Board of Directors' meeting to review registration statement and take other actions related to the offering, including to authorize filing of the registration statement and listing on NASDAQ or an exchange Authorize any Blue Sky filing Appoint pricing committee, and authorize other actions necessary to complete offering Authorize corporate housekeeping	ABC, CC, U
February 3	Year ended December 31, audited financial statements available and provided to printer	ABC, A
February 4–5	All hands meetings: Review printer's proof of registration statements Discuss any discrepancies between text of registration statement and financial statements Finalize underwriting documents	All
February 4–5	Discuss items to include in auditor comfort letter and auditing procedures	ABC, UC, A
February 5	File underwriting agreement with FINRA File listing application with exchange or NASDAQ Make any required Blue Sky filing	ABC, CC U ABC, CC UC
February 6	Begin road show presentation preparation and rehearsal	ABC, U
March 7–8	SEC comments received	All
March 9–10	Appropriate changes made in registration statement or SEC comments otherwise addressed; miscellaneous discussions with SEC staff regarding comments	All
March 13	All hands meeting to review first amendment to registration statements; discuss other issues; review underwriting agreement, etc.	All
March 14	File first amendment with responses to first round of SEC comments Continue road show preparation and rehearsal	ABC, CC, UC ABC, U
March 20	SEC comments on amendment received	All
March 25	Second amendment filed with SEC	ABC, CC, UC
March 26–28	Receive and respond to second/third round of SEC comments File amendment #3/4 to S-1 Finalize road show presentation Set price range	All ABC, CC, UC ABC, U ABC, U
March 28	Board of Directors approve such matters as deemed necessary in connection with the offering	ABC, U
March 29	Distribute Red Herring	U
April 1–5	Road show presentations to underwriters	ABC, U
April 8–12	Road show	ABC, U
April 15	File acceleration requests with SEC	ABC, U
April 16	Registration statement declared effective by SEC	
April 16-17	Pricing agreed upon and approved by ABC Pricing committee Underwriting agreement signed Comfort letter delivered Print and file final prospectus Sales activities commence	ABC, U ABC, U A All C
April 23	Closing	All

Appendix E:

A sample due diligence checklist

I. Financial information

A. Annual and quarterly financial information for the past three years

1. Income statements, balance sheets, cash flows, and footnotes
2. Planned versus actual results
3. Management financial reports
4. Breakdown of sales and gross profit by:
 - a. Product type
 - b. Channel
 - c. Geography
5. Current backlog by customer (if any)
6. Accounts receivable aging schedule

B. Financial projections

1. Quarterly financial projections for the next three fiscal years
 - a. Revenue by product type, customers, and channel
 - b. Full income statements, balance sheets, and cash flow statements
2. Major growth drivers and prospects
3. Predictability of business
4. Business plan, if available
5. Risks attendant to foreign operations (e.g., exchange rate fluctuation, government instability)
6. Industry and company pricing policies
7. Economic assumptions underlying projections (different scenarios based on price and market fluctuations)
8. Explanation of projected capital expenditures, depreciation, and working capital requirements
9. External financing arrangement assumption

C. Capital structure

1. Current shares outstanding
2. Schedule of all options, warrants, rights, and any other potentially dilutive securities with exercise prices and vesting provisions
3. Summary of all debt instruments/bank lines with key terms and conditions
4. Off-balance sheet liabilities

D. Other financial information

1. Taxes
 - a. Summary of current federal, state, and foreign tax positions, including net operating loss carryforwards

- b. Federal, state, local, and foreign tax returns for last 5 fiscal years
 - c. A description of all audits by any federal, state, local, or foreign taxing authorities, including the date and a summary of each audit
 - d. All tax elections filed by the Company or any subsidiary
 - e. All legal or accounting tax opinions received by the Company or any subsidiary during the last five calendar years from outside advisors that relate to any tax reporting matters
2. Discuss general accounting policies (revenue recognition, etc.)
 3. Schedule of financing history for equity, warrants, and debt (date, investors, dollar investment, percentage ownership, implied valuation, and current basis for each round)

II. Products

A. Description of each product (include product literature)

1. Major customers and applications
2. Historical and projected growth rates
3. Market share
4. Speed and nature of technological change
5. Timing of new products, product enhancements
6. Cost structure and profitability

B. Product warranties and liability issues

1. A description of all product warranties relating to any products developed or sold by the Company or any subsidiary
2. Explanation of any product recalls in last five years

III. Customer information

A. List of significant customers for the past two fiscal years and current year to date by application (contact name, address, phone number, product(s) owned, and timing of purchase(s))

B. List of strategic relationships (contact name, phone number, revenue contribution, and marketing agreements)

C. Revenue by customer (name, contact name, phone number for any customers accounting for 5% or more of revenue)

D. Brief description of any significant relationships severed within the last two years

E. List of top 10 suppliers for the past two fiscal years and current year to date with contact information

IV. Competition

A. Description of the competitive landscape within each market segment including:

1. Market position and related strengths and weaknesses as perceived in the market place
2. Basis of competition (e.g., price, service, technology, and distribution)

V. Marketing, sales, and distribution

A. Strategy and implementation

1. Discussion of domestic and international distribution channels, including any VARs or OEMs
2. Positioning of the Company and its products
3. Marketing opportunities/marketing risks
4. Description of marketing programs and examples of recent marketing/product/public relations/media information on the Company

B. Major customers

1. Status and trends of relationships
2. Prospects for future growth and development
3. Pipeline analysis

C. Principal avenues for generating new business

D. Sales force productivity model

1. Compensation
2. Quota average
3. Sales cycle
4. Plan for new hires

E. Ability to implement marketing plan with current and projected budgets

VI. Research and development

A. Description of R&D organization

1. Strategy
2. Key personnel
3. Major activities

B. New product pipeline

1. Status and timing
2. Cost of development
3. Critical technology necessary for implementation
4. Risks

VII. Operations

A. List of properties

B. Summary of supply chain and risks and contingency plans

C. History of any business interruptions

VIII. Management and personnel

A. Organization chart

B. Historical and projected headcount by function and location

C. Summary biographies of senior management, including employment history, age, service with the company, years in current position

D. Compensation arrangements

1. Copies (or summaries) of key employment agreements
2. Benefit plans

E. Discussion of incentive stock plans

F. Significant employee relations problems, past or present; labor contracts

G. Personnel turnover

1. Data for the last two years
2. Key unfilled vacancies

IX. Legal and other matters

A. Pending lawsuits against the company, detail on claimant, claimed damages, brief history, status, anticipated outcome, and name of the company's counsel

B. Pending lawsuits initiated by the company -detail on defendant, claimed damages, brief history, status, anticipated outcome, and the name of company's counsel

C. Description of environmental and employee safety issues and liabilities

1. Safety precautions
2. New regulations and their consequences

D. List of material patents, copyrights, licenses, and trademarks- issued and pending

E. Summary of insurance coverage/any material exposures

F. Summary of material contracts

G. History of SEC or other regulatory agency problem, if any

H. Organization and Standing

1. Articles of incorporation, including amendments
2. Current Bylaws
3. Corporate minute books
4. A list of all jurisdictions in which the Company or any subsidiary owns or leases assets (including real property), has employees or is qualified to do business as a foreign corporation.
5. A list of all current and former subsidiaries of the Company

X. Other company information

A. List of board members

B. List of all shareholders with shareholdings, options, warrants, or notes

Glossary

Acceleration. Procedure in which the SEC declares a registration statement effective, waiving the statutory 20-day waiting period after the registration statement is filed in final form.

Accelerated filer. An issuer after it first meets the following conditions at the end of its fiscal year: (1) public float of \$75 million or more but less than \$700 million at the end of its most recently completed second fiscal quarter; (2) subject to the filing requirements of the 1934 Act for at least 12 months; (3) at least one annual report filed under the 1934 Act, and (4) not eligible to be a smaller reporting company.

Accredited investor. The SEC designation for an individual or entity meeting certain strict criteria. Certain restricted offerings are open only to accredited investors.

Aftermarket. Trading activity in a security immediately following its IPO.

Agreement among underwriters. An agreement signed by the members of the underwriting syndicate, empowering the lead underwriter to sign an underwriting agreement with the company selling the stock (issuer). This is now generally accomplished electronically through standardized document.

All hands meeting. A meeting of all the parties involved in preparing the registration statement (normally company management, company counsel, underwriters, underwriters' counsel, and auditors).

All or none. A best-efforts underwriting agreement in which sales are final only when the entire issue is sold.

Analyst. An individual who studies the development of individual companies or industries for the purpose of advising investors.

Audit committee financial expert. A person who has the following attributes: (1) an understanding of generally accepted accounting principles and financial statements; (2) the ability to assess the general application of such principles in connection with the accounting for estimates, accruals, and reserves; (3) experience preparing, auditing, analyzing, or evaluating financial statements that present a breadth and level of complexity of issues that can reasonably be expected to be raised by the issuer's financial statements, or experience actively supervising one or more persons engaged in such activities; (4) an understanding of internal control over financial reporting; and (5) an understanding of audit committee functions.

Bailout. An offering in which the selling shareholders are perceived to be selling their interests because of a loss of confidence in the company's potential.

Best efforts. An underwriting agreement in which the underwriters agree to use their "best" efforts to sell the issue (without any up-front financial commitment), acting only as agents of the issuer.

Bid and asked. The quoted prices for trading in the OTC market. The bid is the highest price someone is willing to pay; the asked is the lowest price at which someone will sell.

Blue Sky laws. A popular name for the various states' securities laws that have been enacted to regulate and supervise the offering and sale of securities in that particular state. The National Securities Markets Improvement Act (NSMIA) has preempted the registration requirements of the Blue Sky laws for many IPOs.

Bring-down comfort letter. The update to the comfort letter issued as a condition of closing an offering. The bring-down letter reaffirms the detailed comfort letter issued when the offering becomes effective.

Broker. An individual or firm that acts as an intermediary between a buyer and a seller, usually charging a commission.

Broker-dealer. An individual or firm in the business of buying and selling securities for itself and others. When acting as a broker, a broker-dealer executes orders on behalf of its clients. When acting as a dealer, a broker-dealer executes trades for its firm's own account, for which such securities may be sold to clients or other firms or become a part of the firm's holdings.

Capitalization. The total amount of the various securities issued by a company. For registration-statement purposes, capitalization includes all short- and long-term debt and shareholders' equity.

Closing. A meeting at the conclusion of an offering, held for the purpose of completing the issuance and sale of the stock. It includes delivery of a number of documents, including certifications, legal opinions, and bring-down comfort letter.

Comfort letter. A letter provided by the auditors to the underwriters, indicating the results of agreed-upon procedures performed on financial data, included in the registration statement (other than the audited financial statements), as requested by the underwriters.

Confidential treatment. The method whereby a company can request that certain sensitive or confidential information contained in exhibits to filings made with the SEC be redacted from the documents and not made available to the public.

Dealers. Individuals or firms in the securities business who buy securities for their own account and sell to customers from inventory.

Dilution. The reduction of one's relative interest; the sale of additional shares dilutes the percentage of one's ownership. Also, a disclosure in the registration statement comparing the offering price to the tangible book value per share of the company's stock before and after the offering.

Directors' questionnaires. Questionnaires circulated by company counsel and underwriters counsel before registration. The questionnaires verify information about the directors that is to be disclosed in the registration statement.

Due diligence. An investigation conducted by the parties involved in preparing a registration statement to form a reasonable basis for believing that the statements contained therein are true and that no material facts are omitted.

Electronic Data Gathering, Analysis, and Retrieval (EDGAR). An electronic system developed by the SEC. EDGAR became operational in 1995, and allows companies to file SEC documents that are required to be filed electronically. The site can be visited via the SEC's website at www.sec.gov.

Effective date. The date on which the registration statement is declared effective by the SEC and the sale of securities can commence.

Financial printer. A printer who specializes in the printing of financial documents, including prospectuses and registration statements.

FINRA. The Financial Industry Regulatory Authority is the largest self-regulatory organization for the securities industry in the U.S. and provides oversight of brokerage firms. It also performs market regulation under contract for, among others, NASDAQ. FINRA reviews underwriters' compensation to determine whether underwriting agreements are fair and reasonable.

Firm commitment. An underwriting agreement in which the underwriters agree to buy the entire issue and then resell it.

Foreign Corrupt Practices Act (FCPA). Provisions within the 1934 Act that require companies to maintain adequate records and systems of internal control with regard to certain foreign payments. Also prohibits bribery of foreign governmental officials in order to obtain or retain business.

Foreign private issuer. A company that is incorporated or organized under the laws of a foreign country, except an issuer meeting the following conditions: (1) more than 50% of the issuer's outstanding voting securities are directly or indirectly held by residents of the U.S. and (2) any of the following: (a) the majority of the executive officers and directors are U.S. citizens or residents; (b) more than 50% of the assets of the issuer are located in the U.S.; or (c) the business of the issuer is administered principally in the U.S.

Form 8-K. Current report required to be filed with the SEC by most domestic companies when specific material events or corporate changes occur.

Form F-1. Basic registration form used to register securities by foreign private issuers.

Form S-1. The most commonly used SEC form for registering securities in an IPO.

Form 6-K. Current report required to be furnished by foreign private issuers with the SEC material information (1) distributed to shareholders or filed with a foreign stock exchange, if made public by that exchange; or (2) required to be made public by its domestic laws.

Form 8-A. The registration form under the 1934 Act to register a class of securities under the 1934 Act to allow trading to occur.

Form 10-K. Annual report required to be filed with the SEC by domestic companies in compliance with the 1934 Act.

Form 10-Q. Quarterly report, containing primarily unaudited quarterly financial information, which must be filed by domestic companies with the SEC in compliance with the 1934 Act.

Form 20-F. Unlike other SEC Forms, this Form is both a registration and annual report form used by foreign private issuers under the 1934 Act.

Free writing prospectus. Written communications that constitute offers to sell the issuer's securities after the filing of a registration statement other than the statutory prospectus or certain post-effective communications.

Green shoe. An option in a firm commitment underwriting agreement allowing the underwriters to purchase additional shares of stock from the issuer or the selling shareholders to cover over-allotments.

Gun Jumping. Communications in advance of the filing of a registration statement designed to prepare or "condition" the market for the offering in violation of the 1933 Act.

International Financial Reporting Standards (IFRS). A set of accounting standards developed by the International Accounting Standards Board (IASB) used in many countries globally.

Independent director. A member of the company's Board of Directors who is not an employee of the company or any subsidiary and who does not have a relationship which, in compliance with the requirements of the listing exchange independence rules and in the opinion of the company's Board of Directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director.

Insider. Officer, director, or a 10% shareholder of a public company.

Insider trading. The purchase or sale of the company's stock by directors, officers, and others with access to material nonpublic information about the company.

Institutional investor. A bank, mutual fund, pension fund, or other corporate entity that trades securities in large volumes.

Investment banker. The intermediary between the company issuing new securities and the investing public. Also known as an underwriter.

IPO. Initial public offering. An issuer's first public distribution of a security.

Large accelerated filer. An issuer after it first meets the following conditions as of the end of its fiscal year:

- (1) Public float of \$700 million or more as of the last business day of its most recently completed second fiscal quarter;
- (2) subject to the filing requirements of the 1934 Act for at least 12 months;
- (3) at least one annual report filed under the 1934 Act; and
- (4) not eligible to be a smaller reporting company.

Lead or managing underwriter. The investment bank, which has the primary responsibility for organizing a stock issue. The lead underwriter forms an underwriting syndicate, advises on the pricing and timing of the issue, ensures demand for the securities by promoting them, and organizes the road show.

Legend stock. See restricted stock.

Letter of intent. A generally nonbinding letter from the underwriters to the issuer, confirming the underwriters' intent to proceed with an offering and the general terms of the underwriting agreement.

Lock-up agreement. An agreement with underwriters whereby certain shareholders may not sell their shares in the company for a period of time after the effective date of a registration statement (usually lasting 180 days).

Making a market. Efforts by a dealer to maintain trading activity in a particular stock by offering firm bid and asked prices in that stock.

Market maker. A dealer who maintains firm bid and offering prices by standing ready to buy or sell at publicly quoted prices in a particular security.

Material information. Refers to information that a reasonably prudent investor would find of importance in making an investment decision.

NASDAQ. The National Association of Securities Dealers Automated Quotations is the world's largest computer-based stock market that includes the NASDAQ Global Select Market, NASDAQ Global Market, and the NASDAQ Capital Market.

Nonaccelerated filer. An issuer that does not meet the definition of an accelerated filer or a large accelerated filer.

NYSE. The New York Stock Exchange is the largest stock exchange (non-electronic) in the U.S.

Officers' questionnaires. Questionnaires circulated by company counsel and underwriters' counsel before registration to verify information about the officers that is to be disclosed in the registration statement.

Over-allotment. A practice in which underwriters offer and sell more shares than they have agreed to buy from the issuer.

Over-the-counter (OTC) market. A market made up of dealers who buy and sell securities not listed on an exchange. The OTC market relies on telephone sales rather

than on the auctions found on exchanges.

Partial secondary offering. An offering in which securities are offered for sale by both the company and existing shareholders.

Price-earnings ratio. A measurement of stock value calculated by dividing the price per share of common stock by earnings per share.

Primary offering. An offering in which previously unissued securities are offered for sale by a company.

Private placement. An offering of securities exempt from registration, which is limited in distribution.

Prospectus. The official document included in the registration statement filed with SEC, used as the selling document in an offering that discloses pertinent information regarding the issuer and the securities being sold. It must be given (or deemed given) to original purchasers of the security no later than with the confirmation of their purchase.

Proxy solicitation. The request to be authorized to vote on someone else's behalf. A proxy statement must be furnished to shareholders before soliciting their proxies.

Proxy statement. A document which the SEC requires a company to send to its shareholders that provides material facts concerning matters on which the shareholders will vote.

Public Company Accounting Oversight Board (PCAOB).

A private-sector, nonprofit corporation, created by the Sarbanes-Oxley Act, to oversee the auditors of public companies in order to protect the interests of investors and further the public interest in the preparation of informative, fair, and independent audit reports.

Public float. The aggregate market value of the issuer's outstanding voting and nonvoting common equity held by nonaffiliates.

Quiet period. Generally, the period between the time the registration statement is filed and the later of the pricing of the offering and the effective date, so called because of the restrictions on publicity. There are also restrictions on publicity both before and after the quiet period

Red herring. A preliminary prospectus, circulated during the waiting period, which bears a legend in red ink stating that the registration statement has not yet become effective.

Registrar. An agency that issues certificates to new shareholders and checks the transfers of stock to make sure that the number of new shares issued is the same as the number of shares canceled.

Registration. The administrative procedure for filing information required under the 1933 Act.

Registration statement. A document filed with the SEC to register securities under the 1933 Act. The statement (e.g., Form S-1) comprises the prospectus and other information not required in the prospectus.

Regulation D. Provisions of the 1933 Act that contain some of the rules governing private-placement offerings.

Regulation Fair Disclosure (FD). The rule governing selective disclosure by issuers of material nonpublic information, requiring that when an issuer or person acting on its behalf discloses material nonpublic information to certain enumerated persons, it must disclose that information simultaneously for intentional disclosures or promptly for nonintentional disclosures by a method or methods reasonably designed to effect broad, nonexclusionary distribution of the information to the public.

Regulation S-K. The primary integrated disclosure rules for preparing the portions (other than the financial statements) of forms filed under the 1933 and 1934 Acts.

Regulation S-X. The primary rules governing the preparation of the financial statements in documents filed under the 1933 and 1934 Acts.

Restricted stock. Securities, usually issued in a private placement, that have limited transferability. Also called legend stock or lettered stock.

Road show. A series of presentations by company executives during the waiting period, for the purpose of introducing the company and its management to potential investors, analysts, and underwriters.

Rule 144. An exemption provided in the 1933 Act that allows, under certain conditions, the sale of restricted stock and other stock by controlling persons in the public market without registration of that stock.

Rule 144A. An exemption provision of the 1933 Act that provides “safe harbor,” under certain conditions, for resales of securities to certain qualified institutional buyers.

Sarbanes-Oxley Act of 2002. Congress enacted reforms aimed at restoring investor confidence which will hold public companies to a higher standard of corporate governance than in the past.

SEC. The Securities and Exchange Commission is a federal agency created by the 1934 Act, to administer federal securities laws.

Secondary offering. An offering in which securities of previously unregistered stock are offered for sale by existing shareholders.

Securities Act of 1933, as amended (1933 Act). Sets forth the disclosure and antifraud requirements for securities offered and sold in interstate commerce and through the mails.

Securities Exchange Act of 1934, as amended (1934 Act). Regulates and controls the securities markets and related practices and matters. Includes ongoing disclosure requirements and antifraud provisions.

Short sale. A sale of securities that are not owned by the selling party. In anticipation of a decline in prices, a seller sells short and borrows securities to make delivery. The seller

later buys shares to replace those shares borrowed and, if the price did in fact decline, makes a profit.

Short-swing profits. The profits from trading in the company’s stock realized by directors, officers, and 10% shareholders of a company within any six-month period.

Smaller reporting company: A company that meets all of the following criteria: is not an investment company, an asset-backed issuer, or the majority-owned subsidiary of a parent that was not a smaller reporting company; had a public float of less than \$75 million as of the last business day of its most recently completed second fiscal quarter, and in the case of an issuer whose public float was zero, had annual revenues of less than \$50 million during its most recently completed fiscal year for which audited financial statements are available on the date of filing.

Stabilization. Attempts by the underwriters to stabilize prices during the distribution of a new issue, specifically through the purchase of securities for their own account when the market price is at a dip below the public offering price.

Syndicate. A group of investment bankers who together underwrite and distribute an offering of securities.

Tender offer. A formal offer to purchase shares of stock from existing shareholders, usually in connection with an attempt to gain control of the company.

Tombstone ad. An advertisement announcing an offering of securities and indicating where a copy of the prospectus can be obtained.

Transfer agent. An agency that keeps the official records of the names and addresses of a company’s shareholders and handles the transfer of shares from one person to another.

Underwriter. See investment banker.

Underwriters’ discount. A percentage of the gross proceeds of an IPO that constitutes the compensation paid to the underwriters for marketing and selling the offering.

Underwriters’ questionnaire. Questionnaire circulated to all prospective members of the underwriting syndicate to obtain information regarding the names and addresses of the underwriters, any relationships with the issuer, stock ownership, and so forth.

Underwriting agreement. An agreement between a company and its underwriters, setting forth the terms of the offering, including method of underwriting, the offering price, and commissions.

Waiting period. The period between the date the registration statement is initially filed with the SEC and the date it is declared effective.

Window. That period of time when the public market is anticipated to be receptive to the purchase of new securities.

XBRL. Stands for eXtensible Business Reporting Language and is a language for the electronic communication of business and financial data.

Financial Accounting and Reporting Services

Deloitte & Touche LLP

Transparency, timeliness, and accuracy in financial reporting are considered essential attributes in business and financial reports are closely scrutinized by investors, analysts, and regulators alike. Deloitte & Touche LLP's Financial Accounting & Reporting Services (FARS) assists organizations with their efforts to meet financial reporting requirements, including the preparation of financial statements and regulatory filings, and the application and implementation of complex accounting standards for U.S. GAAP and IFRS (International Financial Reporting Standards).

FARS offers a dedicated group of professionals with extensive IPO experience across all industries. FARS professionals have advised numerous companies through the successful completion of their offerings. FARS professionals have broad knowledge of applicable SEC rules and regulations, disclosure requirements, and global accounting principles, and work closely with companies and their advisors to assist in the public offering process.

Our services include:

- Assisting company management with SEC reporting requirements and in assessing the company's disclosures, and making recommendations on financial disclosures required within a registration statement
- Assisting companies in evaluating new and revised accounting principles
- Interacting with the company and its advisors on financial accounting and SEC reporting matters
- Assisting with the review of drafts of the prospectus or offering memorandum
- Advising companies in connection with ongoing SEC financial reporting obligations
- Assisting the company and its advisors in responding to comments received from the SEC

Deloitte has a range of publications and resources to assist with SEC-related matters, including Deloitte's SEC Reporting Interpretations Manual, and our Dbriefs series. See the next page for a listing of SEC related publications.

Contact the specialists:

Tom Omberg

Partner, New York
Leader, Financial Accounting
& Reporting Services
Deloitte & Touche LLP
+1 212 436 4126
tomberg@deloitte.com

Jack Azose

Partner, New York
Deloitte & Touche LLP
+1 212 436 4838
jazose@deloitte.com

Howard Cohen

Director, New York
Deloitte & Touche LLP
+1 212 436 5454
howcohen@deloitte.com

Sam Doolittle

Partner, San Francisco
Deloitte & Touche LLP
+1 415 783 4343
sdoolittle@deloitte.com

Deloitte & Touche LLP ("Deloitte & Touche") is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. The information contained in this publication is subject to changes and Deloitte & Touche is under no obligation to update such information. Before making any decision or taking any action that might affect your interests, you should consult a qualified professional advisor. Deloitte & Touche is not responsible for any loss sustained by any person who relies on this publication.

Deloitte publications

In addition to this guidebook, Deloitte has a range of publications to assist with SEC-related matters. These publications can be found at www.deloitte.com. These include

Heads Up Newsletters:

SEC Issues Financial Reporting Manual
SEC Publishes Final Rule Mandating Use of “Interactive Data”
SEC Modernizes Oil and Gas Company Reporting
Study Finalized on Mark-to-Market Accounting
SEC Approves Rules Requiring Registrants to Submit Interactive Data
Highlights of the 2008 AICPA National Conference on Current SEC and PCAOB Developments
SEC Issues Proposed IFRS Roadmap
SEC Proposes to Give Certain U.S. Issuers the Option to Use IFRSs and Proposes a Roadmap to a Mandatory Transition Date for All U.S. Issuers
SEC Holds Fourth Roundtable on IFRSs
Complexity DeClifired — SEC Advisory Committee Releases Final Report
Something to Talk About — SEC Staff Explains the Filing Review and Comment Letter Process
Great “X”pectations — SEC Proposes Mandating XBRL Use to Make Financial Data Interactive
Regulations Committee and SEC Staff Hold First Meeting of 2008
DeClifiring Complexity — SEC Advisory Committee Releases Progress Report
Highlights of the 2007 AICPA National Conference on Current SEC and PCAOB Developments
SEC Holds Roundtables on IFRSs
Major Changes to Business Combination Accounting as FASB and IASB Substantially Converge Standards
XBRL U.S. GAAP Taxonomy Made Available for Public Comment
SEC Removes Reconciliation Requirement, Approves Smaller Public Company Rules
SEC Regulations Committee and SEC Staff Hold Third Meeting of 2007
ESOARS Take Off — SEC OKs Use of a Surrogate to Value Employee Share Options
SEC Feedback on Executive Compensation Disclosures: “Where’s the Analysis?”

SEC Staff Issues Comment Letters on Executive Compensation Disclosures
The Shift Toward IFRSs and Its Impact on U.S. Companies
SEC Regulations Committee and SEC Staff Hold Second Meeting of 2007
SEC Provides Further Relief for Smaller Public Companies
SEC Proposes Easing Requirements for Foreign Filings
SEC Tackles a Wide Range of Topics
SEC and PCAOB Approve New Section 404 Guidance: No Additional Delay for Nonaccelerated Filers
Expected SEC Actions Will Increase Relevance of IFRSs in the U.S.
SEC Regulations Committee and SEC Staff Hold First Meeting of 2007
SEC Discusses Improvements to Section 404 of the Sarbanes-Oxley Act
SEC Clarifies Views on the Design of Market-Based Employee Stock Option Valuation Model
Matching Critical Terms in Hedge Strategies — Major Accounting Firms Discuss Ramifications With SEC Staff
SEC and PCAOB Update
09-4: SEC Further Defers Section 404(b) Requirement for Nonaccelerated Filers

Financial reporting alerts:

09-3: SEC Advises Registrants to Further Explain Provisions and Allowances for Loan Losses in MD&A
08-16 (Revised): SEC Issues Letter Clarifying Other-Than-Temporary Impairment Guidance for Perpetual Preferred Securities
08-11: SEC and FASB Release Fair Value Clarifications
08-10: SEC Advises Registrants to Further Explain Fair Value in MD&A — An Addendum to the March 2008 SEC Letter
08-7: SEC Advises Registrants to Further Explain Fair Value in MD&A
08-1: SEC Issues Letter Clarifying Accounting Ramifications of Accelerated Efforts to Mitigate Subprime Crisis
07-10: SEC Extends the Use of the Simplified Method in SAB 107 Under Certain Circumstances
07-5: CAQ Update — Key Accounting Issues and the Credit Environment
07-4: Key Accounting Issues and the Current Credit Environment

Did you know...?

Deloitte’s SEC Reporting Interpretations Manual includes interpretive guidance and more than 125 Q&As on the following topics:

- *Understanding the SEC.*
- *Business combinations* — Providing financial statements of an acquired business required under Regulation S-X, Rule 3-05.
- *Unconsolidated subsidiaries and equity method investees* — Providing financial information of unconsolidated subsidiaries and equity method investees required under Regulation S-X, Rules 3-09 and 4-08(g).
- *Real estate operations* — Providing financial information of acquired real estate operations required under Regulation S-X, Rule 3-14.
- Registrant’s financial statements.
- *Guarantor financial statements* — Providing guarantor financial statements required under Regulation S-X, Rule 3-10.

The SEC Reporting Interpretations Manual is available on Technical Library: The Deloitte Accounting Research Tool. For more information, including subscription details and an online demonstration, visit www.deloitte.com/us/techlibrary.

In addition, in August 2009, Deloitte added *SEC Reporting for Business Combinations and Related Topics — A Roadmap to Applying SEC Regulation S-X to the Acquisition of a Business* to its Roadmap series. When a registrant acquires, or it is probable that it will acquire, a significant business or real estate operation (acquiree), it may be required to provide separate financial statements of the acquiree and pro forma financial information in a Form 8-K, registration statement, or proxy statement. This new roadmap is a valuable tool for understanding the related SEC reporting considerations. In addition, the roadmap covers how certain provisions of ASC 805 (formerly Statement 141(R)) affect the SEC reporting considerations for business combinations. The codified roadmap features an executive summary as well as over 100 Deloitte interpretive Q&As.

Deloitte refers to one or more of Deloitte Touche Tohmatsu, a Swiss Verein, and its network of member firms, each of which is a legally separate and independent entity. Please see www.deloitte.com/about for a detailed description of the legal structure of Deloitte Touche Tohmatsu and its member firms. Please see www.deloitte.com/us/about for a detailed description of the legal structure of Deloitte LLP and its subsidiaries.

Copyright © 2010 Deloitte Development LLC. All rights reserved.
Member of Deloitte Touche Tohmatsu