

Trial by IPO

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An initial public offering (IPO) of a company's stock to the investing public stresses a CEO, CFO and other senior managers. Even though a corporate communications department is typically on the periphery of the action leading to an IPO, stress can drive a corporate communications director into tension as well. The push to produce the thick S-1 Registration statement for the Securities and Exchange Commission (SEC) in order to sell stock, the Road Show to introduce the company to investors, pricing and start of trading are fraught with unknowns resolved under tight deadlines. Surviving the pressure requires patience and endurance until lawyers, investment bankers, accountants, Board members, the SEC and others are satisfied. An IPO is so time-consuming that normal communications activity with top management falls away. The regulatory "Quiet Period" that surrounds an IPO constrains what can be said, and interpretation of "Quiet Period" guidelines creates tension between the General Counsel and corporate communicator.

More profoundly, going public changes corporate communications. There is need for greater transparency, for more disclosure and for accountability to investors. This creates a swing in communications from silence during the IPO to intense demand for information after the IPO. Communications directors have to guard against

cessation of normal communications while preparing for an onslaught.

An IPO usually begins with whispers about discussions to go public. The communications director may or may not be privy to conversations in the Boardroom. The CEO, CFO and/or Board discuss the future and growth of the firm and whether the company is best served by selling shares to the public or by remaining private. In some cases, the CEO has intended to take a company public from the day it was founded. In other cases, need for money to sustain growth pushes a private company into public markets. Discussions may last for days or months depending on management's views, the market and the condition the company's company. Rumors may fly for a long time before there is action.

The first concrete step is selection of an underwriter (investment banker) who will sell the stock. This is sometimes called a "Beauty Pageant." When this happens, the company is serious about going public. The CEO, CFO and Board meet with investment bankers and choose one on the basis of criteria such as:

- Experience the underwriter has with similar companies.
- An estimate of the money the underwriter might raise for the company.

- The ability of the underwriter to market the shares.
- The reputation of underwriter in the financial marketplace.

In most cases, the underwriter makes a firm commitment to purchase all shares (called a “bought deal”) at a discount from the company then resell them at full price to institutional investors and individual investors. It’s a multi-step process. The company sells shares to the underwriter. The underwriter in turn sells shares directly to the public and to other investment banks that in turn sell the shares to the public. This transfers the risk of selling the shares to the underwriter, who in turn gets rid of some of the risk by selling shares to other investment banks. The underwriter sets up a syndicate of investment banks to market the shares right away. The syndicate gathers information from clients to determine interest and initial demand for the shares. Effective communications are at the core of an IPO, and underwriters are skilled in listening to investors and in presenting a company’s case persuasively. Another decision taken during this initial period is where to list the company’s shares. There are two major markets left in U.S. -- the New York Stock Exchange and the NASDAQ, the world’s largest electronic stock market. The NYSE has more stringent requirements for listing than the NASDAQ.

IPO madness begins with an “all hands” meeting. Company management meets with attorneys who will help them write the S-1 Registration statement for the SEC, underwriters who will also draft language and manage the sale and independent auditors who examine company financials. After this meeting, a race to the offering begins. From this

day until after the stock is listed, the CEO, CFO and other senior managers are likely to be preoccupied and less available unless a communications issue is related directly to the IPO.

The Quiet Period is a major challenge facing a corporate communications director. This is a prolonged period of silence imposed on companies about to sell and after selling common stock to prevent them from hyping the stock and fooling investors. The General Counsel is largely in charge of communications during the Quiet Period, which lasts from the time the company announces that it is going public until nearly a month after an IPO is completed. The General Counsel must make sure that no communications occur that might prevent the IPO; that there is no offer orally or in writing to sell securities publicly except by registration statement and no reference to the IPO in public beyond a brief announcement that the company intends to file. Attempts to flack a company’s stock before the company goes public is called “gun jumping,” and the SEC takes a dim view of it.

Essentially, officers, directors or employees are barred from talking about the company or its present or future financial condition in speeches, articles, on TV or radio or on the Internet. That said, the rules state that the company can continue normal communications activities. For a company that has been active in communications, there is the rub. What constitutes normal and extraordinary communications is a daily issue. This requires that the corporate communications director work with the General Counsel. Basically, General Counsel are of two types. The Counsel

with a light hand sets clear guidelines, orders one to follow them and lets the corporate communications director operate. The Counsel with the heavy hand demands that every communication go through the Counsel, which, of course bogs the communications flow because the Counsel is busy with many things during an IPO. The corporate communications director unfortunately does choose the Counsel, so in spite of best efforts to keep regular communications programs going, a heavy-handed Counsel might shut them down during the Quiet Period. There is little that one can do except to appeal to the CEO, who can overrule the General Counsel, but CEOs may not choose to do so.

An IPO is total immersion for company management and key employees. It is typically a 100-day madness in which every element of the company is examined, verified and written into the S-1 Registration. The reason for such intense focus is that each party in an IPO may be legally liable for false statements. There is an incentive to be right. The analysis, called Due Diligence, commences when attorneys for the underwriters or company present a list of documents they need to review. The company must respond to all questions as fully and accurately as possible. This touches off a race to the records for significant contracts, details of executive compensation, status of pending lawsuits, revelations about ownership and potential conflicts of interest and a great deal more. It is time consuming and costly, but underwriters and attorneys reduce their liability by learning all they can about the company, its business, its management and its financial condition. Due diligence does not end until the

SEC declares a registration statement effective.

The S-1 Registration has enormous value to the corporate communications director because it is a compendium of company facts that investors need to know before buying a company's shares. Every S-1 has a:

- Prospectus summary, a précis of the company's business, terms of the offering and financial condition of the company. (This is the first section prospective investors review, and it is usually rewritten many times before finalized.)
- Risk factors that give all the reasons why a company might fail. These are so voluminous that they sometimes reach a level of absurdity, but attorneys who write them seem to abide by a "better-safe-than-sorry" principle.
- A discuss of capitalization and indebtedness, including use of the proceeds from selling shares.
- Management's discussion and analysis of financial condition.
- A business discussion that detail operations, strategy, current situation and probable trends in the company's industry, competitors, manufacturing capabilities, employees, lawsuits, intellectual property and regulations impacting the business.
- A section on management that provides information about directors and officers,
- A section on principal shareholders
- Other information and exhibits that are not part of the cut-down version of the S-1 given to investors and called the prospectus.

An S-1 Registration is a committee document to which everyone contributes, and it incorporates a multiplicity of interests. Attorneys, underwriters, the company and auditors all have overlapping roles. Underwriters push to market the stock. Attorneys push to limit risk. The company pushes its point of view. The auditor pushes to get accurate financials according to U.S. Generally Accepted Accounting Principles. As a result there is inherent tension in the completion of the document with negotiation over what is said and how it is presented. What emerges is a compromise written in language that is flat and factual. The company makes an initial filing of the S-1 with the SEC. The SEC examines it and sends a written response about a month after the filing that asks for additions or revisions. Requests for more information can be picayune or substantive, and revisions may take days or weeks. When everyone is satisfied the S-1 is close to completion, the underwriter prints a prospectus to use in marketing the stock. This is called the Red Herring after the warning printed in red on the cover to alert investors that the S-1 is not final and is subject to change.

While this going on, production of the “Road Show” presentation begins, and here the corporate communications director may be pulled in to help. The Road Show is a whirlwind and grueling series of meetings in a week or two that take the CEO and CFO to all major U.S. and some Europe cities to meet investors and tell the company’s story. The presentation is a sales tool. The underwriter will take a large hand in how the company’s story is told. Completing the presentation can be a torture of seemingly endless negotiation between

what the CEO wants to say, what the underwriter wants, what the Board thinks is important, what the CFO has to get into the presentation of the financials and what others chime in to add. Revision piles on revision until everyone is satisfied or runs out of time. Even then, the underwriter will warn that the presentation will be changed while the Road Show is underway to reflect investor questions and concerns. Along with the Road Show presentation are questions investors are likely to be asked with answers. These amount to dozens of potential questions that can catch the company off guard or somehow diminish the story. The corporate communicator is likely to help with collection of questions and phrasing of answers. During this time, the CEO and CFO rehearse the presentation and changes. It will be one of the most important presentations they will make to investors and how they perform is crucial to acceptance or rejection of the new issue.

The corporate communications director and investor relations specialist (perhaps newly appointed) will be busy getting ready for the first day of trading. There is usually a ceremony. The New York Stock Exchange has a series of events that begins with a breakfast, presentations and climaxes with ringing of the bell above the exchange floor to commence trading. Companies also are invited to display products, to provide giveaways to the traders and to conduct other celebratory activities. The corporate communications director should have plenty of time to plan and implement these. In addition, there will be interviews with the media, messages to employees and customers and others informing them of the company’s new status. The difficulty of preparing is that

it will not be clear when trading will start. In addition to these tasks, the corporate communications director should evaluate how corporate communications will function once the company is public. The company could be understaffed in communications, or its staffing may need to be realigned. Meanwhile the corporate communications director and the investor relations specialist need to produce an investor relations Web page, identify analysts who are likely to follow the stock, prepare media lists and attend to essential items such as working with the transfer agent that takes care of physical stock distribution.

Once the Road Show is done and the SEC has approved the S-1, the underwriter can seek accelerated approval to set a specific date when the listing will take place. When that happens, everything goes into higher gear. In the final hours before listing, the underwriter sets the price for the shares to be sold. Often this is done after the closing of the market the day before trading begins. Because the price determines how much money the company will raise, this is an excruciating time. If the price is too high, the stock will be rejected. If the price is too low, the stock will trade much higher than the share price and the company has lost out on millions of dollars that it might have raised. The underwriter uses information collected from the syndicate, feedback from investors and gut instinct to settle on a final share price. As a precaution, the company usually gives the underwriter a “green shoe” option. This permits the underwriter to buy more shares within a short period of time in order to help stabilize the price of the stock after it starts trading.

Opening of trading is filled with tension. The stock could trade at a huge premium, or pop, over the share price. It could to everyone’s horror “break” and trade below the share price or it could trade within a comfortable range above the share price, such as a 15% premium. Everyone will watch until trading settles into a pattern and price range. Then it is back into the Quiet Period for 25 more days. But this is a time when the corporate communications director begins to implement plans for general and trade media and other briefings to introduce the company all around. While the company may have been known as a private firm, there is even greater interest as a public firm. And, because the company is newly listed, it is the perfect opportunity to tell the company’s story again. This has the effect of getting the company “on the radar” with reporters, analysts and others who will follow it. It will also increase requests for information and for inclusion in news stories that it might not have gotten as a private firm.

Life for the corporate communications director is different in a public company. There is greater need to disclose what the company is doing, a greater attention from the media and investor interest. One has to deal as well with how the CEO views communications. Some CEOs see no need for enhancing communications. Others want to broaden communications. But life is different if for nothing else, the trial a company undergoes to sell common stock publicly.

Jim Horton started his career in Investor Relations and assists companies undergoing IPOs.