

Going Public In the New Millennium: New Rules – Old Touchstones

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During the 1990s, hundreds of companies rode the IPO wave. They quickly raised — and quickly burned through — billions.

Today, going public still provides companies a unique path for raising needed cash and providing long-term liquidity. However, going public in the new millennium will be decidedly different. A company must first ask whether it makes sense to consider going public.

For many small and mid-cap companies, being a public company today is like being in limbo. No analysts follow their stock, trading volume is low, the stock price languishes, stock options are under water and there is little hope of subsequent offerings. Most problematic is that compliance with the Sarbanes-Oxley Act is triggering additional annual costs estimated to be more than \$1 million. Not surprisingly, many of these companies are pursuing the option of going private.

Given this new environment, the bar for going public is higher. Many investment bankers are advising that it simply does not make sense to go public unless a company has growing annual revenues approaching \$100 million, near-term profitability and is seeking to raise at least \$50 million.

Enterprises with the best IPO prospects these days have a solid business model, visibility on several quarters of increasing revenue and profitability, strong management teams and market leadership.

Before launching an IPO, a company must understand what it is facing. Being public has always had drawbacks, including the challenge of running a business in a fishbowl, meeting market expectations and compliance burdens. With Sarbanes, the disadvantages have multiplied considerably. Among the requirements of Sarbanes are:

- A majority of the board must be inde-

pendent

- At least one board member must meet stringent standards of financial expertise

- The board generally must have audit, compensation and nominating committees composed exclusively of independent directors

- The CEO and CFO are required to “personally certify” the company’s financials

- Internal financial and disclosure controls must be maintained and assessed by management and future management’s report must be attested to by outside auditors

- Whistleblower protection policies must be instituted.

Senior management and the directors will need to devote more time to corporate governance. Also, to attract qualified directors, companies will need to pay them more and maintain adequate directors and officers insurance, the premiums for which can easily exceed \$100,000.

Those who conclude that the benefits of being public outweigh its costs should prepare long before the IPO process begins. Necessary preparation includes designing and implementing financial and disclosure controls, producing clean financial statements, developing the capability to make accurate disclosure, building a strong management group, and assembling a team of experienced advisors, including accountants, lawyers and investment bankers.

In the wake of perceived abuses, a blue ribbon advisory committee recently recommended no fewer than 20 specific changes to the IPO process.

In the new rigorous climate of the post-Sarbanes era, companies pursuing a public offering will need to return to the old touchstones: necessary capital for growth, currency for future acquisitions, and recurring value for stockholders.

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