



IPO SERIES: TO, THROUGH AND BEYOND THE IPO

UNDERWRITER SELECTION AND ROLE

Tapping the financial markets through an IPO is both an exciting and challenging task. You have chosen professionals for your legal and financial matters, and now you need to add the expertise of a transfer agent. In this series – “To, Through and Beyond the IPO” – EQ shares its deep expertise and insights into the entire process as a private company goes public.

01 THE UNDERWRITER’S CENTRAL ROLE

The first step in the IPO process is for the issuing company to choose an investment bank to advise the company on its IPO and to provide underwriting services. Selecting the underwriter is the foremost initial step in going public.

As a financial expert who specializes in IPOs, the underwriter will be there at all the key steps involved in going IPO, from the SEC registration process to pricing shares to the market stabilization and transition of the company. Given the criticality of the underwriter’s ongoing role throughout the process, you’ll work closely with and rely on your outside counsel for the selection of the best underwriter to guide your company to public life.

02 WHO IS THE UNDERWRITER?

Generally, the underwriter is an investment bank with IPO specialists. The investment bank will ensure that all regulatory requirements are met, including filing with appropriate agencies, deposit of all fees, and public availability of all requisite financial data about the firm.

The next and possibly the most important action for the underwriter is to contact and engage large prospective buyers able to purchase significant quantities of the company’s stock. These large institutional investors may include endowment funds, hedge funds, mutual funds, pension funds, and insurance companies.

Based on an assessment of prospective buyers’ appetite for the stock, the underwriter will recommend an IPO price. Shares will be sold at this price. If priced too high, the company risks being saddled with unsold stock. If priced too low, potential revenue is sacrificed. The underwriter’s balancing act is to gauge what the market will support, establish a viable price, and come in neither too high nor too low in order to make the IPO as financially successful as possible.

03 CHOOSING THE RIGHT UNDERWRITER

Like interviewing job applicants, generally you and your outside counsel will meet with several candidates – teams of investment bankers – as you review their qualifications, expertise, and “fit” as a member of your team. Given the close working relationship that will be necessary, you’ll want a partner who’s right for you and your needs. Some factors you’ll want to pay specific attention to include the following:

- **Experience.** Be certain the bank has experience in your industry. Has it previously managed IPOs for companies in your sector? Were the results successful? Hard facts and data can support the bank’s credentials to serve you well in the IPO.
- **Logistical considerations.** What are the underwriter’s strengths and weaknesses? What is the level of its capabilities in areas such as research and marketing? Learn which research analysts will be assigned, their reputations, and whether they have worked together before. An effective team is key.
- **Preliminary valuation.** The bank will prepare a preliminary valuation of your company based on your financials. An assumed growth rate of both the company and industry, and the price/earnings ratio for comparable issuers, will provide critical underlying assumptions for the preliminary valuation.

When the time comes to make a decision, the final selection criteria will come down to such critical factors as:

- Reputation
- Research quality
- Industry background, knowledge, and expertise
- Distribution capabilities (which investment bank is most likely to sell the greatest number of shares)
- Your prior relationship, if any, with the bank

04 UNDERWRITER GUARANTEE

For your protection, the investment bank generally furnishes a guarantee to the company that commits to sale of a specific quantity of stock. The underwriter also commits to purchase unsold shares itself. The guarantee provides an important impetus for the underwriter to meet its commitment and avoid having to buy the shares it was unable to sell.

The underwriter guarantee is an important safety net for the company going IPO, and it equally serves as motivation to the underwriter. While the bank can sell these shares on the open market, it may be more prudent not to have them in the first place since the stock price may decrease due both to having unsold shares from the IPO and then flooding the market with them. This undermines the issuer’s value while the bank will take a loss in this situation too.

05 DUE DILIGENCE AND FILINGS

As one of the first activities performed directly after selection and engagement, the underwriter will draft the following documents. Please note individual details and documents will vary for a specific IPO.

Engagement Letter

- Reimbursement clause
- Gross spread/underwriting discount
- Gross spread is the difference between the price at which the underwriter purchases the issues and the price at which they sell the issues.

Letter of Intent

- Underwriter's commitment to perform underwriter services to company

Underwriting Agreement

- The Letter of Intent remains in effect until the pricing of the securities, after which the Underwriting Agreement is executed. Thereafter, the underwriter is contractually bound to purchase the issue from the company at a specific price.

Registration Statement

- The prospectus
- Provided to every investor who buys the issued security
- Comprises information that is provided to the SEC for inspection but is not necessarily made available to the public

Red Herring Document

- Initial prospectus created by the underwriter
- Used to market shares to public investors ahead of IPO date
- 3-to-4 week period where underwriters market the shares (Pre-IPO roadshows) to institutional investors to evaluate demand for the future issuance

06 YOU'RE ON YOUR WAY!

With the underwriter on your team and moving you through the IPO process, you are truly on your way to becoming a public company!

About Us

EQ are specialists in helping you better understand and manage the ownership of your company through critical events across the corporate lifecycle. As trusted advisors, we provide strategic insight and operations expertise through our core business units in Private Company Services, Transfer Agent Services, Employee Plan Solutions, Proxy Services, and Bankruptcy. Globally we serve 6,700 clients (47% of the FTSE 100 UK and 35% of the S&P 500), with over 30 million shareholders, through 6,500 employees in 5 markets around the world.

Contact Us

We would welcome the opportunity to meet and provide more information on the full range of our IPO Services and how we can help before, during, and after the IPO. Please contact us at newbusiness@equiniti.com

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