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IPO "An American Perspective"

What an IPO could do for your business

Philipp Harper

If you think initial public offerings are only for big businesses, think again.

Depending on short-term needs and long-term goals — and investor interest in your product or service — an IPO can be a smart move for small and midsized companies.

Consider issuing stock if you're looking for a way to:

- Provide an exit strategy to investors who will feel better about giving you money if there's a market for the equity they hold.
- Position your company for eventual expansion into national or international markets.
- Aggressively boost personal wealth.

Of course, there are costs associated with doing an IPO, both financial and in terms of the time and effort required. And never forget that "being public" means being held to a level of accountability far and above that to which privately owned firms are held.

Expectations should be tempered, too, by the lessons learned from the bursting of the late 1990s' tech bubble. Long gone are the days when a 20-something armed with a good idea and a better line could raise tens of millions in venture financing, enlist the services of a major league underwriter and in short order debut on the NASDAQ.

Know who your investors are up front

Generally speaking, entrepreneurs should not consider going public unless they know who their investors will be, says Michael Williams, a Tampa-based securities lawyer specializing in small-business IPOs.

Except in the most overheated markets, "there is virtually no broker-dealer or other legitimate money-raising organization willing to raise money for small business," he says. "Brokerage firms like to raise $50 million a shot, not $1 million."

Any entrepreneur who envisions taking an unsuspecting market by storm on the strength of a good idea probably is ignoring reality. Says Williams: "This is not a field of dreams, where if you build it they will come."

However, taking a small business public may make perfect sense if the goal is to create a market for investors who already have put money in the business or who have expressed a willingness to do so. Indeed, ensuring that investors have an exit strategy when they want to cash out makes it easier to attract money in the first place.
But remember, knowing up front where the investment capital is coming from is paramount. "Don't go through the process unless you know the answer to that question," Williams says. "It's not worth it." Business owners who can answer that question affirmatively shouldn't be

reluctant to go public because of the size of their business or because it's not in a "hot" sector. Among the small businesses Williams has helped go public are a leasing company, an Internet marketer, a developer of anti-piracy software and a dry cleaning franchisor. The amount of money raised has ranged from $150,000 to $1 million.

Can you afford to do it? Do you really need to?

The availability of financing isn't the only thing to consider when deciding whether to issue stock. Two other thresholds need to be cleared as well, says Stephen Brock, CEO of gopublictoday.com, a Las Vegas-based investment advisory firm specializing in direct public offerings by small businesses.

First is the matter of capability. Does the business have the wherewithal both to go public and then to stay public? If a company lacks the resources required to tell its story in a compelling way, selling its shares probably will be an uphill fight. And assuming the transition to public status is made successfully, the business owner must then contend with the legal and accounting costs associated with regulatory compliance. Those costs can be significant.

Second, what operational scope does the entrepreneur envision for the business? "Are you out for a national or international footprint?" Brock asks. "If you plan to stay within one state, forget it. You'll end up with shares that will never go anywhere."

Going public also can make sense if the business owner has aggressive growth in mind. The ability to issue stock rather than cash for an acquisition is a powerful finance tool.

Costs versus payoff

Once the decision is made to go public, there are a number of registration vehicles that can be used. Which is most appropriate varies from company to company, and with the exchange where the stock will be listed.

The OTC (over the counter) Bulletin Board and the Pink Sheets (also an OTC exchange) are where most small-business stocks are traded. The Pink Sheets is considered by far the more speculative of the two, and as such requires less in the way of financial reporting and disclosure. (The NASDAQ, of course, is a more prestigious but also a much pricier and more rigorous alternative.)

All registrations are subject to federal and state securities laws as well as industry regulation. It's worth noting that certain states are considered more IPO-friendly than others — among them, Nevada, Colorado and New York.

Stock registration is not a do-it-yourself enterprise. Attorneys or other consultants specializing in small-business IPOs almost always are needed to make it though the process, which can be costly in terms of both money and time.

Once filed, a registration generally takes three to six months to be approved. And a considerable pre-filing period may be needed to bring a small company's financial reporting capabilities up to snuff. "Most small businesses have not kept their books or run the business in an auditable fashion," Williams says.

And the expense? According to a Government Accounting Office study of small-business IPOs undertaken in the 1994-99 period, figure to spend about 10% of what you expect to raise with the issue. Costs vary of course from case to case and exchange to exchange. Brock estimates that an OTC Bulletin Board listing is twice as expensive as one on the Pink Sheets. Williams says the least-expensive listing on the Pink Sheets will cost about $75,000.

The hoped-for pot of gold at the end of the rainbow is the form of a higher valuation for the company, one pegged to market capitalization as opposed to just assets. Says Brock: "You get more value built quickly."