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Initial public offering in the USA is attractive for German companies

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In Germany, innovative business models are usually financed by private equity and late-stage growth capital. The capital market plays a subordinated role. However, a listing on the NYSE or NASDAQ is a promising step for fast growing companies.

With the 2012 Jumpstart Our Business Startups Act (JOBS Act), the US set the conditions for young, fast growing companies to access the capital markets. Since then, the number of small-to-medium-cap listings gives evidence that the US stock markets can be an attractive marketplace across all industries for companies with innovative and profitable business models, even from overseas.

Advantages for foreign issuers

Foreign private issuers (FPIs), i.e. companies whose shareholders and/or assets are primarily located outside the USA, can profit substantially from such US listings.

- Before the public filing, the SEC discusses the drafts of the prospectus and/or the application for listing on the stock exchange with the issuer on a confidential basis.
- When it comes to submitting the financial records, the issuer may limit itself to two past consequential financial years.
- There is no requirement to submit an audit certificate for the published financial statements.
- The issuer is allowed to conduct “test-the-water” communications with potential investors to sound out their interest in subscribing shares.
- After the IPO, there is generally a reduced disclosure obligation on the part of the issuer.
- The reporting obligations regarding directors’ and officers’ dealings are relatively light.

Before making the decision regarding an US IPO, the company should make a reliable projection regarding the chances of a pricing and completion of an IPO. This does not refer to the legal form, corporate governance or articles of association of the FPI, as German stock corporations are not required to undergo any change in that regard. Aside from assimilation to an US issuer, e.g. in view of a code of conduct/compliance program and employee stock option programs, what matters more than anything for the risks and rewards of a US offering are hard market criteria:

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- Steady growth of the company in revenue over a five-year period at least;
- The current and future material relevance of the NAFTA countries in terms of sales and markets for the product portfolio and business model of the company;
- Evaluation arbitrage in comparing with competitors or peers headquartered in the USA using sales and income indices as well as leverage (indebtedness as a multiple);
- Liquidity of the US public capital markets and a positive outlook regarding the IPO window;
- Scope and depth of the sector and market research as well as strong analyst coverage;
- Volume of primary and/or secondary offering against background of requirements in terms of the size of the free float on NASDAQ and NYSE;
- The entire cost of a US listing (about 10% of the proceeds of the flotation).

Preparation of the US listing

If the projection is positive, the next step is to select the underwriting banks. What really matters for the decision in allocating the roles between lead and co-book runner as well as the further underwriters is placement power, sector and industry knowledge, quality of the analyst coverage and also reliability in legal execution. A strong track record and sound understanding of the nature of cross-border IPOs are indispensable.

Any work on the prospectus and the registration statement must be preceded by a comprehensive due diligence. The diligence exercise may be carried out in parallel by advisers of the company and the underwriting banks. The market, company history, risk factors, business model and corporate governance must be described in detail in the prospectus and the registration statement, addressing in particular all of the relevant cross-border and multijurisdictional aspects.

The listing application is followed by a four-week waiting period during which the SEC examines the registration statement. Fairly regularly, the SEC enters into a lively dialogue with the issuer in order to clarify potential misunderstandings or to have the company explain the business model and the home country rules in more detail. With the listing application the project is also published on the SEC website (EDGAR).

Aside from the mandatory conversion of the issuer's financial statements under German GAAP to IFRS, the way the financial statements are to be presented to the public is new to most European issuers.

US Trading currency via ADRs

The shares of an FPI cannot be traded in the US easily as a matter of principle. It is therefore necessary to create a tradable US security by way of American depository receipts (sog. übertragbare Hinterlegungsscheine), which represent the shares. This creates a complex triangular relationship under German civil law between the issuer, a US depository bank and a European based custodian bank which holds the shares in custody for the US depository bank. Detailed handling and custody agreements are executed for such American depository receipts program, which shall secure all rights deriving from the shares in general shareholder meetings in particular.

Conclusion: By experience, six to nine months must be planned for the entire process from the kick-off meeting with the underwriters to the pricing and flotation of the shares. During this time the issuer will have to devote substantial internal resources to the process, with the pricing and successful listing on a US stock exchange on the finish line.

**) Berthold Hummel, a partner with Dechert LLP, specializes in corporate and equity capital market law and has been active in the VC and private equity industry advising clients for more than 18 years. Under his leadership, a team of German and US Dechert lawyers handled the listing of German voxeljet AG, a manufacturer of industrial 3D printers, on the NYSE back in October 2013. The total number of shares issued resulted in approximately 100 million US\$ of listing proceeds.*