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Challenges for European companies considering an IPO abroad

The finance department's perspective

The preparation and implementation of an IPO itself is already a major challenge. Due to significant disclosure requirements and fixed due dates for external reporting, internal processes have to be optimized. Or they may even have to be created for the first time – both when going public and remaining public. A company may decide for strategic reasons – e.g., increased visibility, better access to industry-specific investors and consequently better pre-money valuation – not to follow the well-known path to the European stock markets. If the company instead chooses an IPO in the world's most important capital market, which is in the U.S., it will have to meet additional requirements and also analyze alternatives for action. **By Ulrich Sommer**

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This article presents a brief overview of the challenges of a U.S. IPO, which companies should take into consideration in their decision-making process and project planning.

Choosing the right entry into the U.S. capital market

U.S. stock market regulations explicitly provide for foreign companies' participation in the U.S. capital market. In addition to having a direct public offering in the U.S., foreign companies have the right to offer securities to a narrow circle of qualified institutional investors on the basis of Rule 144 A of the U.S. Securities and Exchange Commission, which includes some simplification rules over direct listing. This option becomes relevant if the original listing is outside the U.S. Another alternative is listing American depositary receipts (ADRs), which represent non-U.S. securities – e.g., shares of European companies – that are qualified for trading on U.S. financial markets.

In a direct listing on the U.S. stock market, the candidate is either a Domestic Registrant (DR) or a Foreign Private Issuer (FPI). When deciding how the IPO is structured, the company must carefully consider which of these two it will be incorporated as. In particular, it is imperative to decide if the listing should be accomplished with a U.S. Inc. or a European parent company. Generally, the requirements for a DR are stricter than for an FPI. This applies, for example, to the accounting standards, which must comply with US GAAP if DR is chosen. For an FPI, IFRS or even the locally accepted accounting standards accompanied by a reconciliation calculation to US GAAP are allowed. Also with regard to the reporting requirements and the reporting deadlines, the FPI status is less strict. Other relief is provided in the form of the Jumpstart Our

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> *Relief is provided in the form of the Jumpstart Our Business Startups (JOBS) Act for companies below a certain size.*

Business Startups (JOBS) Act for companies below a certain size (EGC – Emerging Growth Companies). Key points are the following: Financial information for only two full years must be disclosed; it is possible to file registration statements confidentially, and the internal control system (SOX Compliance) is part of the annual audits and includes an initial time delay. Provisions such as those accorded by FPI status and the JOBS Act are not offered on European exchanges for the Prime Segment and should therefore be play a role in the decision-making process for a U.S. listing.

Additional challenges

Once the decision about the IPO procedure has been made, a basis for the financials required must be built within the accounting system. Audited financial statements provide the foundation for this; they can be prepared in accordance with local GAAP, although a conversion to US GAAP or IFRS is compulsory.

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Audited historical financial statements usually do not meet the strict mandatory regulations of the Public Company Accounting Oversight Board (PCAOB). If the auditors can comply with the PCAOB requirements early in the process, a lot of time can be saved in the IPO preparation phase. Another main challenge for project management is the necessary coordination of internal resources, auditors and the SEC lawyers working for the company. In contrast to the procedure in Europe, SEC lawyers are not only involved in creating listing documents but are also actively involved in reviewing financial statements. To avoid expensive and time-consuming review loops, a close coordination of involved parties and frequent regular meetings are necessary. Furthermore, one should not underestimate the complexities caused by converting accounting – whether out of necessity or strategy – from the international Euro to the U.S. dollar, especially in terms of preparing all registration documents and carrying out investor relations work. The strict PCOAB tests and the lack of limitation of liability for auditors in the U.S. also lead to significantly higher audit costs. Furthermore, the considerably higher fees of U.S. attorneys, in particular of capital market lawyers, need to be included in calculations. Finally, the main advantage of the U.S. capital market, i.e., the access to a broad investor base, is something that must literally be acquired.

Conclusion

Deciding to have any kind of IPO means that the IPO candidate must have high standards for its internal organizational structure. Thus, choosing an IPO in the United States, which lies outside the more familiar European stock market environment, increases demands on project management considerably and greatly broadens the scope of documents that must be prepared. Strong arguments for a U.S. listing, however, include advantageous regulatory differences, visibility in the world's most important capital market, increased reputation and, most notably, access to a wider circle of industry-specific and financially strong investors. Yet a U.S. IPO comes with elevated effort and cost. ■