www.teknosassociates.com
info@teknosassociates.com

Revised Valuation Allows Completion of IPO

Because of SEC questions about stock option grants made in the year before an IPO filing, a Silicon Valley company was unable to complete its offering. Teknos was hired to redo several valuations, "cheap stock" charges were calculated, and a new prospectus was filed – the SEC gave its approval just days later.

SEC questions about options had delayed a company's IPO by 90 days and there was no end in sight

CHALLENGE

A young, fast growing Silicon Valley semiconductor company filed a registration statement with the SEC in order to go public. Normally, the SEC reviews a prospectus in less than 90 days and provides its comments. Typically, there is some discussion about the comments, the company makes some changes in its filing, the SEC agrees to these, and the company is free to begin marketing its stock in the "road show."

In this case, the SEC asked pointed questions about the pricing of stock options granted to employees during the year before the filing. The accounting staff at the SEC objected to the low prices of the grants and had issues with the valuation reports which had been used to support those prices. In essence, the SEC wanted the company to take larger "cheap stock" charges. The valuation firm was unwilling to get on the phone and defend its work to the SEC, so the process was at a standstill. What should have taken three months had been dragged out to six months – with no end in sight – and the condition of the IPO market was deteriorating.

SOLUTION

At the recommendation of the IPO company's law firm, we were consulted about the problem. We met with management of the company, examined the prospectus and the valuation reports which had been challenged by the SEC, and devised a plan to get the IPO process back on track.

Analysis of Situation

The earlier valuation reports contained problems because they had been prepared by a large, generalist valuation firm with little knowledge about technology companies: the reports used only one valuation approach, comparison to publicly traded companies, and there was no analysis of discounted cash flows or examination of sales of preferred stock; plus the publicly traded company analysis included only three semiconductor companies, all of which produced products very different from the IPO company . Finally, the large, generalist valuation firm had a policy of not speaking with the SEC in order to justify its work or answer questions.

Teknos recommended that new valuation reports be prepared. We suggested a discounted cash flow analysis and some consideration of recent sales of preferred stock, plus altering the list of publicly traded companies to include more – and more relevant – comparable companies. Management of the IPO company agreed, as did the company's audit and law firms.

New Valuation Reports

Working over a few days, we prepared three new valuation reports for various dates during the year preceding the IPO filing date. Understandably, the common stock values indicated by the new reports differed from the values in the earlier reports and this created "cheap stock" charges.

The "cheap stock" charges were incorporated in the IPO company's financial statements and approved by the audit firm. The IPO company's law firm revised the registration statement and filed it with the SEC. A few days later, there was a conference call with the accounting staff at the SEC. We participated in the call and answered questions.   Two days after that, the SEC informed the IPO company that it had no further comments on the prospectus. The IPO company began its "road show" the next day and completed its offering two weeks later. Less than one month after that, conditions in the IPO market deteriorated so greatly that an offering probably could not have been completed.

Teknos Associates is a valuation firm which serves emerging growth companies and their venture capital backers. We are a team of experienced and credentialed valuation professionals with backgrounds in appraisal, accounting, investment banking, and venture capital.

We provide appraisals to facilitate compliance with a variety of tax and accounting requirements, including option issuance and portfolio valuation. We support merger and acquisition activities with independent fairness opinions. And we offer valuations of intangible assets and liabilities after an acquisition.

We have produced hundreds of valuation reports quickly and economically, without sacrificing quality. Our reports have stood up to scrutiny by Big Four audit firms, the IRS, and the SEC. Contact us at to see how we can help you.