IPO Bound?
New Strategies, New Ideas and Tips for Success

Legal, audit and accounting experts share frontline insights

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Speakers

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Agenda

- Welcome/Objectives
- JOBS Acts – New Path to IPO
- Three Phases to an IPO
- IPO Readiness
- Some Key Practice Concerns for your IPO
- Final Remarks

Objectives

- Provide an overview of the JOBS Act implications for IPO
- Share best practices and advice for preparing and conducting an IPO
  - Accounting considerations
  - IPO Readiness considerations (finance, governance, controls)
  - Legal considerations
- Review timeline and planning guidelines
- Amplify key points with some real-life scenarios

JOBS Act

Jumpstart Our Business Startups Act

JOBS Act: *Summary*

- Signed into Law April 5, 2012
- Purpose: To increase American job creation and economic growth by improving access to the public capital markets for emerging growth companies

JOBS Act: *Emerging Growth Co.*

- Annual gross revenue < $1 billion
- EGC status is retained for 5 years <u>unless:</u>
  - Becomes a large accelerated filer ($700 million public float)
  - Annual revenues > $1 billion in most recent fiscal year
  - Issues > $1 billion in nonconvertible securities over a rolling 3-year period
- Registrants with a common equity IPO on or before December 8, 2011 are not eligible

JOBS Act: *IPO On-Ramp*

- Confidential review of draft registration statement
- Reduced disclosure requirements
  - 2 years of financial statements
  - Private company timeline for compliance with new accounting pronouncements
  - Allowed to provide smaller reporting company compensation disclosures
- Allows “test the waters” communications
- Provides greater flexibility for sell side research
- Delayed Sox 404(b) – auditor attestation

JOBS Act: *Other Key Provisions*

- Increased record holder threshold from 500 people to 2,000 (or 500 non-accredited investors) and exclude employees from record holders
- Rule 506 exemption
  - General solicitation permitted
  - <u>Only</u> accredited investors
- Provides structure for crowdfunding

Three Phases of an IPO

Important finance & accounting considerations

Kelley P. Wall

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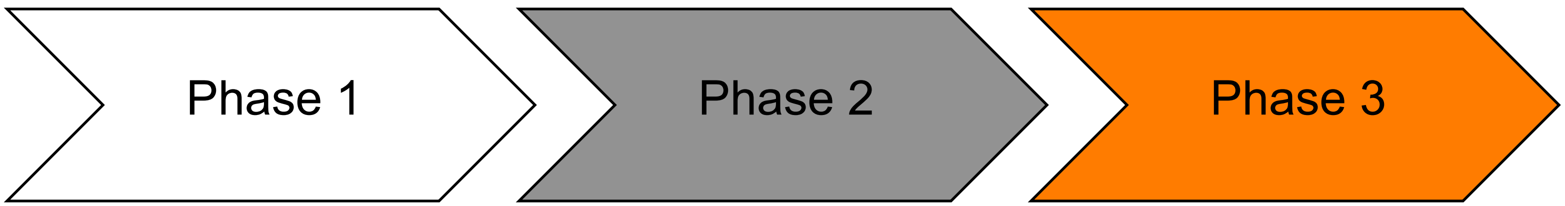
IPO Phases

1-2 years prior to IPO	IPO Process	Newly Public



Phase 1 (1-2 years prior to IPO)

- Systems
- Equity
- Internal controls
- Streamline close
- Financial audits
- Technical accounting

Phase 2 (IPO Process)

- Data warehouse
- Team / roles
- Timeline
- Messaging
- SEC response team

Phase 3 (Newly Public)

- Equity
- Earnings release
- SEC reporting

Keys to Success - Phase 1

- Consider system capabilities & scalability
- Get your equity documentation in order
- Assess internal controls
- Close your books like a public company
- Complete financial statement audits / plan for quarterly reviews
- Address & document technical accounting issues
- Plan for increased workload

Keys to Success - Phase 2

- Pull finance agreements for data warehouse
- Finance & accounting are important contributors to the cross-functional team
  - Ensure roles & responsibilities are clearly defined
  - Help set a realistic timetable
- The registration statement is a collaborative document
  - Review non-financial sections for accounting/reporting issues
  - Consider ongoing reporting obligations for financial metrics & messaging
- Establish an SEC response team

Keys to Success - Phase 3

- Allocate time to equity
  - Stock plan registration statements
  - Employee communication
  - Transfer agent / stock broker collaboration
- Establish earnings release process
  - Team & responsibilities
  - Timetable
  - Management reporting needs
- Build external reporting roles & responsibilities
  - Disclosure Committee
  - Management certifications
  - XBRL reporting requirements

Critical Timing Considerations

- Plan ahead & work backward from target IPO date
- Coordinate timing with significant company events, tradeshows, product introductions, etc.
- Complete major corporate projects prior to Phase 2
- Plan around international holidays
- Consider the *age* of your financial statements
- Coordinate timing with your auditors in advance
- Remember: SEC review is generally 3-4 months

IPO Readiness

Finance, Governance, and Control Considerations

Ernst & Young

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Preparing for the IPO
The value proposition

The IPO should be a structured and managed process, which begins long before the transaction. We refer to this process as The IPO Value Journey®, a transformation involving the people, processes and culture of an organization. Successful IPO companies begin acting like a public company at least a full year prior to going public.

The value proposition: Invest in people, process and technology

- **Reduce execution risk**
  - Reduce the risk that your company is not adequately prepared for the IPO transaction and life thereafter as a public company.
  - Ensure business execution will continue apace, despite the focus on the IPO transaction
- **Increase market perception**
  - Improve the perception of your business and brand with investors, customers, suppliers and employees
- **Facilitate regulatory compliance**
  - Increase rigor and focus on public company operating and reporting requirements imposed by the SEC and Sarbanes Oxley.
- **Increase performance**
  - Align resources, business processes and infrastructure to support both the long-term growth strategy as well as improve operational effectiveness.
  - Prepare to provide guidance that will meet or beat market expectations

Areas of accounting complexity
Leading causes of financial restatements

Topic	Percentage of restatements
Income taxes / deferred taxes	19%
Statement of cash flows	11%
Revenue recognition	9%
Allowances	4%
Leases	4%
Stockholders' equity	4%
Business combinations	3%
Derivatives	3%
Liabilities	3%
Balance sheet / income statement reclassifications	3%

Top three matters represent nearly 40% of all restatements

Sarbanes-Oxley Act Summary

What's Required?

Reporting: Upgrade Disclosures

Section 302
Management certification of filing accuracy and control effectiveness

Section 401
Disclosures of off B/S transactions and pro forma financial information

Section 404
Management report and auditor attestation on effectiveness of internal controls over financial reporting

Section 409
Disclosures of material changes in financial conditions or operations

Roles: Strengthen Governa

Section 204
Increased communications between auditor and audit committee

Section 301
- Audit committee directly responsible to select & oversee auditors
- Audit committee only independent directors
- Hotlines, whistle-blower procedures

Section 402
Prohibits loans to officers and directors

Section 407
Disclosure financial expert on audit committee

Conduct: Expand Accountabili

Section 303
Unlawful to fraudulently mislead auditors

Section 306
Prohibition of insider trades during pension blackout periods

Section 403
Accelerated reporting of trades by insiders

Section 406
Disclosure regarding code of ethics and changes or waivers to such codes

Section 806
Whistleblower protections

Enforcement: Increase Oversigh

Section 101 & 102
- Public accounting firms register with and supply information to PCAOB
- Audit firms pay PCAOB annual fees

Section 104
PCAOB conducts regular inspections of accounting firms

Section 108 & 109
Issuers pay annual fees to support FASB and PCAOB

Section 307
Attorneys must report evidence of violation of securities law

Section 408
Expanded SEC review of 10-K's and 10-Q's at least once every three years

Penalties: Broaden Sanctions

Section 304
CEO & CFO forfeiture of bonuses /profits if restatement due to SOX non-compliance

Section 804
Extends statute of limitations for litigation alleging fraud

Section 906
Increased criminal penalties for CEO/CFO who certifies the filing in bad faith

Section 1102
- Criminal penalties for corrupting documents
- Criminal penalties for obstructing proceeding

Section 105 & 802
Penalize accountants' failure to cooperate in investigation, including destruction of W/P's

Relationships: Auditor Independen

Section 201
Prohibits auditor from providing a variety of non-audit services

Section 202
Requires pre-approval by Audit Committee of all services by audit firm

Section 203
Five year rotation of audit partners

Section 206
Requires cooling off period before a member of the audit team can be hired into a Financial Reporting Oversight Role

Preparing for an IPO
Answering the key questions

- Is your financial reporting process public-company ready?
- Are you Sarbanes-Oxley ready?
- Have you implemented effective corporate governance and risk management programs?
- Can your IT systems support your growth strategies and reporting and compliance requirements?
- Have you established an internal audit function?
- Does your FP&A function enable you to manage your business and provide reliable financial guidance?

Preparing for an IPO
The "Dual Track" Approach

- Pros and Cons
  - Flexibility, leverage, possibility of "complete" exit
  - Management distraction, competing priorities, resource drain
- Other considerations
  - Long-term vs. short-term business strategy
  - Key stake-holder priorities
    - Nature of liquidity event (cash versus stock)
    - Employee compensation arrangements
  - Creating the data room – preparing for financial and tax due diligence
  - Compliance matters – SOX readiness, statutory compliance

SOME KEY PRACTICAL CONCERNS FOR YOUR IPO

FENWICK & WEST LLP
Daniel J. Winnike

FENWICK & WEST LLP

Build Thoughtful Projections to Share with Bankers

- Need well-thought, defensible business model projecting quarterly operating results for at least the next 24 months to share with investment bankers and analysts
- Consider sharing useful financial information such as:
- Operating results relative to plan for recent past periods
- Key financial metrics that management uses to track the business
- Critical underpinnings of projections

Get Corporate Housekeeping in Order

- Accurate up-to-date cap table is essential
- Complete corporate minute books
- Identify holes in past corporate proceedings and remediate as best possible
- Identify important subsidiaries
- Qualification to do business in relevant places
- Have current contact information for all stockholders
- Make sure to have cleaned up any issues regarding ownership of your IP

Put a Public company Board of Directors in Place

- Typical Board size would be 5-9 members
- Majority of Directors should be independent
- If CEO is Chairman, name a lead independent director
- Establish Audit, Compensation and Nominating/Governance Committees, with all independent directors
- Virtually all IPO companies have "audit committee financial expert"

Prepare to Identify Executive Officers and Most Highly Compensated Officers

IPO prospectus must identify and provide biographies for "executive officers" and provide compensation information on CEO and two other highest compensated executives. Company must also determine who should be designated as section 16 reporting "officers" (usually same people as executive officers).

Gather Industry Information and Representative Customers Willing to be Identified

Collect data that addresses current and future market size of markets in which company is active.

SEC will allow naming of customers who are representative customers of a product or service of the company.

As a due diligence matter, underwriters will selectively call customers to verify information provided in the prospectus.

Identify Material Agreements and Think About Confidential Treatment

- Material agreements must be filed as exhibits to the registration statement.
- Material agreements may contain technical or pricing information the disclosure of which would be competitively harmful to the company; SEC allows filers to redact very specific items, but must go through a formal CTR process.

Selling Stockholders

In recent IPOs markets seem increasingly amenable to a small portion of the offering coming from existing stockholders, particularly non-management holders with long holding periods.

Substantial logistics are involved, especially as number of participating holders grows.

More companies are planning secondary offerings prior to completion of IPO lock-up period.

Final Thoughts

- 1 Minute Summary from each speaker

Thank you for joining us.
Final Questions?

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- CLE or CPE Credit:
  - Please sign up at registration table