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Considering an IPO?

The costs of going and being public may surprise you

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Contacts

Martyn Curragh
Partner, US Practice Leader, Transaction Services
+646-471-2622
martyn.curragh@us.pwc.com

Henri Leveque
Practice Leader, Capital Markets and Accounting Advisory Services
+678-419-3100
h.a.leveque@us.pwc.com

Neil Dhar
Partner, Transaction Services
Capital Markets Leader
+646-471-3700
neil.dhar@us.pwc.com

Midwest

Mike Gould
Partner, Transaction Services
+312-298-3397
mike.gould@us.pwc.com

West

Joseph Dunleavy
Partner, Transaction Services
+713-356-4034
joseph.p.dunleavy@us.pwc.com

Bryan McLaughlin
Partner, Transaction Services
+408-817-3760
bryan.mclaughlin@us.pwc.com

East

Scott Gehsmann
Partner, Transaction Services
+646-471-8310
scott.j.gehsmann@us.pwc.com

Mike Poirier
Partner, Transaction Services
+617-530-5573
michael.d.poirier@us.pwc.com

New York Metro

Howard Friedman
Partner, Transaction Services
+646-471-5853
howard.m.friedman@us.pwc.com

Embarking upon the IPO process requires insight into the costs

Initial public offerings (IPOs) give companies an opportunity to reinvent themselves. Despite the transformational nature of an IPO, which requires several different parts of the business to work together, many companies embark upon the process without a thorough understanding of the costs. Companies frequently underestimate those costs, as well as the time and complexity associated with this event. According to the results of a recent PwC survey1 on managing the costs of going public, as many as 48% of participating CFOs with firms that had gone public in the United States in the past several years said that the one-time costs associated with their IPOs had exceeded their expectations.

- The magnitude and scope of IPO costs can vary significantly from offering to offering based on a number of variables, such as the size of the offering, the complexity of the IPO structure, and the organization's readiness to be a public company. Factors impacting the cost of an IPO include:

- Direct costs, such as underwriter, external auditor, legal and financial reporting advisor fees

- Longer-term costs such as the need to develop external reporting, investor relations and human resource functions

- Costs to institute incentive plans for executives and employees

Unfortunately, only a portion of the costs incurred as part of the IPO are disclosed publicly, which makes tracking and understanding the costs incurred by other companies that have recently become public difficult.

Before undertaking an IPO, companies must fully consider the costs of the IPO process and the costs of building and maintaining a public company infrastructure. Preparing a detailed analysis of these costs will accelerate the budgeting process and make it more accurate; limit surprises throughout the IPO process; and provide organizations adequate time to develop an infrastructure that will support the rigors and requirements of life as a public company.

Costs directly attributable to an IPO can vary widely based on complexity, size of the company, and a company's readiness to operate in a public environment.

Exhibit 1
Summary of the different types of IPO costs, with illustrative examples and average costs

Going public	Being public
Directly attributable to the offering (netted against proceeds) • Underwriter discount, which based on public registration statements, result in fees equal to 5%-7% of gross proceeds • Legal, accounting and printing fees associated with drafting the registration statement and comfort letter • Road show expenses • In addition to underwriter fees, on average companies incur $3.7 million of costs directly attributable to their IPO	**One-time costs to convert the organization to a public company (expensed as incurred)** • Costs to implement new financial reporting systems and processes • Initial costs to document internal controls and comply with SOX • Costs to identify and recruit a new board of directors • Costs to implement new executive and employee compensation plans • Typically, we estimate companies incur more than $1 million of one-time costs to convert their organization to a public company
Other incremental organizational costs (expensed as incurred) • Tax and legal entity restructuring costs in anticipation of the IPO • Additional audit, interim/quarterly review costs, advisory accounting and other costs to make the financial statements S-X compliant • Valuation reports • Costs to draft new articles of incorporation, audit committee charter, by-laws, and other agreements • Based on our survey results, on average companies incur more than $1 million of one-time costs as a result of going public	**Recurring incremental costs of being a public company (expensed as incurred)** • Incremental internal staffing costs (accounting, tax, legal, human resources, technology, internal audit, and investor relations) • Professional fees for legal and accounting advice • Based on our survey results, on average companies incur $1.5 million of recurring costs as a result of being public

[1] PwC partnered with Oxford Economics on all survey data discussed in this document.

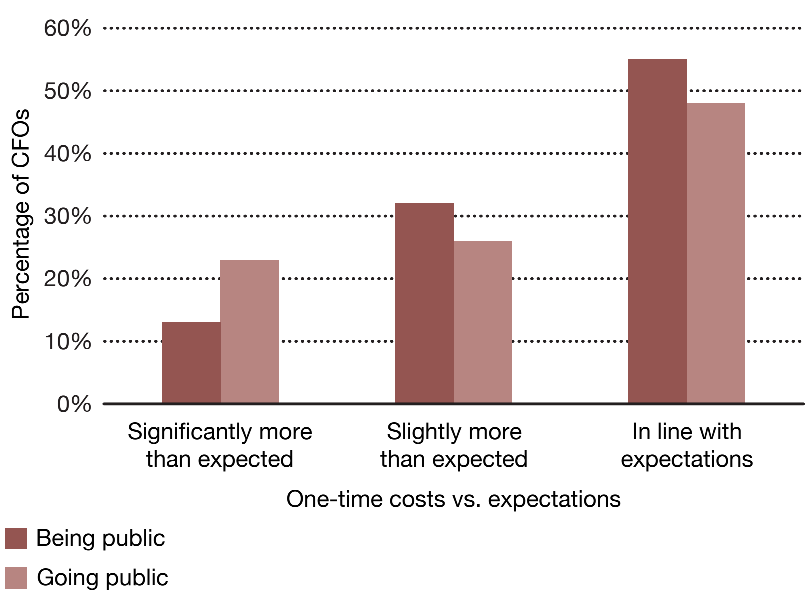
The road to becoming a public company can be long and costly. In fact, 87% of CFOs participating in PwC's recent survey of US firms that have gone public in the past several years indicated that their firms spent more than $1 million on one-time costs associated with the transaction. Our survey indicated that CFOs were more likely to be surprised by the costs of going public than the costs of being public. Specifically, 23% of surveyed CFOs reported that the costs of taking their firm public had exceeded their expectations by a significant amount. In contrast, 13% of the participating CFOs indicated that the costs of managing a public firm were significantly more than they had anticipated before the IPO.

Regardless of the individual nuances that mark a private company's transformation into a new public company, all IPOs share a common thread: a substantial investment in time, money, and resources. To coordinate this undertaking, companies that complete successful IPOs use project management resources to help management as they: build the IPO plan, keep task lists, monitor progress, forecast delivery dates, identify gating issues, and keep decision making on track.

87% of CFOs indicated that their firms spent more than $1 million on one-time costs associated with their IPO.

Exhibit 2

Almost half of CFOs found the one-time costs of going public were higher than they anticipated



The initial public offering

A successful IPO involves two equally important parallel work streams: ***going public*** and ***being public***.

Going public is the process of taking the company through the steps of gathering the necessary financial, marketing, and business information; determining the optimal tax and legal structure; filing the registration statement with the SEC; responding to SEC comments; marketing the business and selling the shares on the road show. The JOBS Act allows certain companies exemptions for some of the disclosures and regulatory requirements associated with an IPO and potentially eases some of the marketing activities. The going public process ends when the offering is sold and the company and/or its shareholders receive the proceeds.

Being public is the process of transforming the organization so that it can operate as a public company. Among the many tasks involved are upgrading, sustaining, or enhancing financial reporting capabilities, creating an investor relations function, meeting the governance, reporting, and internal controls standards and listing requirements of the SEC and of the selected exchange. The JOBS Act temporarily exempts certain companies from the internal control audit requirements of Section 404 of the Sarbanes-Oxley Act, relating to the companies independent auditors; the temporary exemption would not apply to the internal control management reporting requirements of the Sarbanes-Oxley Act.

A comprehensive understanding of the costs involved with an IPO includes the costs associated with both going public and being public.

On average, companies incur $1.5 million of recurring costs as a result of being public.

Exhibit 3:
Timeline of the IPO process

Costs of going public

There are many different costs related to the going public process. For accounting purposes, these costs must be segregated between those that are directly attributable to the registration and offering process (offering costs) and the incremental organizational costs incurred in preparation for the offering.

Accounting concepts: How to account for IPO-related expenses under US GAAP

Many companies working toward an IPO overlook and are unclear about the appropriate way to account for the multitude of expenses that arise during the IPO process. Offering costs are those costs directly incurred in connection with the registration and distribution of the company's shares, while incremental organizational costs may be nonrecurring and can include costs of actually organizing the business entity. A detailed understanding of the applicable accounting guidance is critical, as is a method to accurately segregate and track such costs throughout the IPO process.

Accounting for such costs under US GAAP falls under the following technical literature:

- ASC 720-15–Start-Up Costs
- ASC 340-10-S99-1 (SAB Topic 5.A) — Expenses of the Offering

The SEC has historically taken a fairly strict interpretation of "directly attributable." On several occasions the Staff has questioned the nature of costs that companies have considered directly attributable to an offering.

A comprehensive look at the offering costs incurred during the IPO process

ASC 340-10-S99-1 states that specific incremental costs directly attributable to an offering of equity securities may be deferred and charged against the gross proceeds of the offering as a reduction of additional paid-in capital, and we have seen, through SEC comment letters, that the Staff has taken a fairly strict interpretation of " "directly attributable."

Exhibit 4 summarizes the types of offering costs disclosed in the registration statement.

Exhibit 4
Offering costs disclosed in registration statements

Type of cost	Description
Underwriter's discount	Typically 5% — 7% of gross proceeds.
Legal	Fees from securities counsel to draft the registration statement and provide other advice directly related to the offering.
External auditor	Fees incurred by the independent registered public accounting firm directly related to the offering. These typically include: issuance of the comfort letter, review of the registration statement, and other advice directly related to the offering. Costs not considered directly related to the offering include the cost of year-end audits, including stub-period and re-audits, as well as quarterly reviews.
Financial reporting advisor	Fees incurred by financial reporting advisors directly related to the offering, for example, preparation of the pro forma financial statements, drafting of management's discussion and analysis and other items included within the registration statement, and help in addressing comments from the SEC.
Printing	Document management, SEC filing, printing and distribution expenses.
Registration/other	Registration-related fees and expenses (SEC, state, rating agency).
Exchange listing fees	Fees paid to the New York Stock Exchange (NYSE) or NASDAQ for stock listing services. While there are differences between the two primary exchanges in the US, fees are based on number of shares outstanding and range from $125,000 to $250,000 for initial listing and from $35,000 to $500,000 for annual listing fees.

Treatment of offering costs in an aborted IPO

The accounting treatment of offering costs is contingent on completion of the IPO. If the company does not complete the IPO, ASC 340-10-S99-1 states that the deferred costs of the aborted offering may not be deferred and charged against proceeds of a subsequent offering. Any costs related to an aborted offering should be expensed in the period in which the company elects to abort the offering. A short postponement (up to 90 days) does not represent an aborted offering. Therefore, if the process is slightly delayed, the company can continue to defer offering costs in anticipation of the pending IPO, but significant judgement must be applied to assess the facts and circumstances.

Treatment of IPO costs for tax purposes

Under Treasury Regulation Section 1.263(a)-5(a)(8), all costs incurred in connection with facilitating a stock issuance transaction, of which an IPO would qualify as, must be capitalized under Internal Revenue Code (IRC) Section 263. However, some costs incurred in connection with an IPO are not directly attributable to facilitating the IPO. These costs could qualify for beneficial tax treatment. The following types of costs incurred in connection with an IPO are potentially tax deductible or amortizable:

- Costs incurred in connection with ordinary and necessary business expenses, including employee compensation, business and management plans, ongoing tax advice and public relations expenses. These would be deductible under IRC Section 162.

- Costs incurred in connection with exploring but ultimately not pursuing alternative transactions or financing, such as seeking abandoned financing or pursuing and abandoning separate, non-mutually exclusive transactions. These would be deductible under IRC Section 165.

- Costs incurred in connection with facilitating a borrowing or other tangible/intangible arrangement with a term, including underwriting, commitment, negotiating, structuring and other various financing fees as well as services provided in connection with insurance policies, leases, and other items. These would be capitalized and amortized over the life of the borrowing or arrangement.

Offering costs — Inside the numbers

Based on an analysis of over 380 IPOs between January 1, 2009, and June 30, 2012, the underwriter discount, legal, accounting, and other fees directly attributable to an IPO can result in substantial expenditures. Exhibits 5 and 6 track the range of offering costs companies incur during the IPO process.

Exhibit 5 shows that offering costs, generally, were positively correlated with gross proceeds of the offering. Most notably, underwriter and legal costs trended upward with increased gross proceeds, while accounting costs stabilized for larger deals. These results are not particularly surprising, as accounting costs do not generally increase solely based on deal size, while underwriter fees are tied to the amount of proceeds raised. Printing costs also trended upward for larger deals, likely a result of larger filings and demands on printer resources.

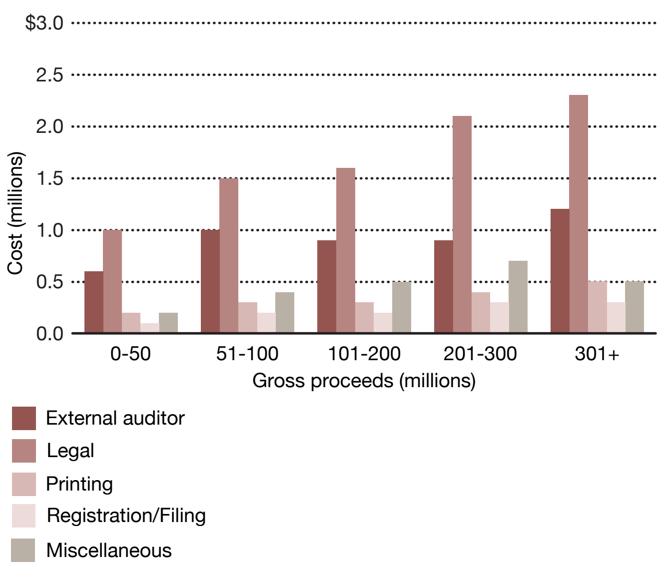
While exhibits 5 and 6 exhibit the range of costs companies may incur, it is very difficult to accurately predict costs without performing a detailed IPO readiness assessment in order to fully understand the nuances and unique complexities companies face during the IPO process. While offering costs vary, as discussed below, a well-prepared company is better able to mitigate the additional expenses and time commitments that could push the IPO process off course.

In a recent PwC survey of newly public companies, 48% of respondents said the cost of doing an IPO exceeded their expectations.

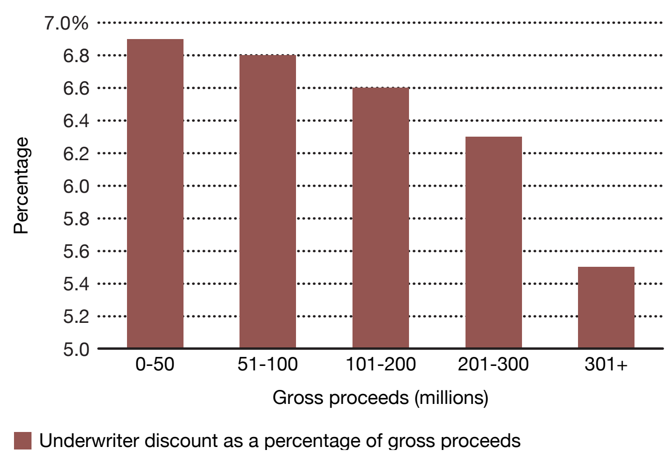
Exhibit 5
Offering costs incurred, based on gross proceeds of offerings

(Numbers in millions, except number of IPOs)		External auditor			Legal			Printing			Registration/ filing			Miscellaneous			Underwriter discount				
Gross proceeds	Number of IPOs	Range		Avg.	Range		Avg.	Range		Avg.	Range		Avg.	Range		Avg.	Range		Avg.	Avg. % of gross proceeds	Avg. total
$0-50	41	$0.0	$2.5	$0.6	$0.1	$4.2	$1.0	$0.0	$0.7	$0.2	$0.0	$0.3	$0.1	$0.0	$0.9	$0.2	$0.2	$3.9	$2.0	6.9%	$4.1
51-100	115	0.0	4.4	1.0	0.3	7.3	1.5	0.1	0.9	0.3	0.0	0.5	0.2	0.0	2.8	0.4	1.2	6.7	5.1	6.8%	8.5
101-200	115	0.1	5.6	1.0	0.2	4.9	1.6	0.1	1.2	0.3	0.0	1.9	0.2	0.0	4.0	0.5	2.5	12.2	9.4	6.6%	13.0
201-300	45	0.1	4.2	0.9	0.6	4.8	2.1	0.0	1.0	0.4	0.1	0.5	0.3	0.0	6.7	0.7	8.0	16.4	15.2	6.3%	19.6
301+	73	0.0	5.0	1.2	0.0	17.0	2.3	0.1	9.8	0.5	0.1	2.4	0.3	0.0	4.5	0.5	7.9	237.9	23.3	5.5%	28.1

IPO costs by gross proceeds



Underwriter discount as a percentage of gross proceeds



As evidenced in Exhibit 6, offering costs of an IPO correlate positively with a company's revenue. In particular, legal and accounting costs, areas where larger companies may face additional complexities in preparing for an IPO, increased significantly for larger companies. Not surprisingly, fees paid to underwriters also increased by revenue category, as larger companies were more likely to have greater equity proceeds and incur higher underwriter costs. Further, the table in Exhibit 6 illustrates the wide range of costs companies will likely incur during the IPO process. For instance, companies with revenues between $501 million and $1 billion incurred legal-related fees ranging from approximately $200,000 to $7.5 million, with an average of approximately $2.6 million.

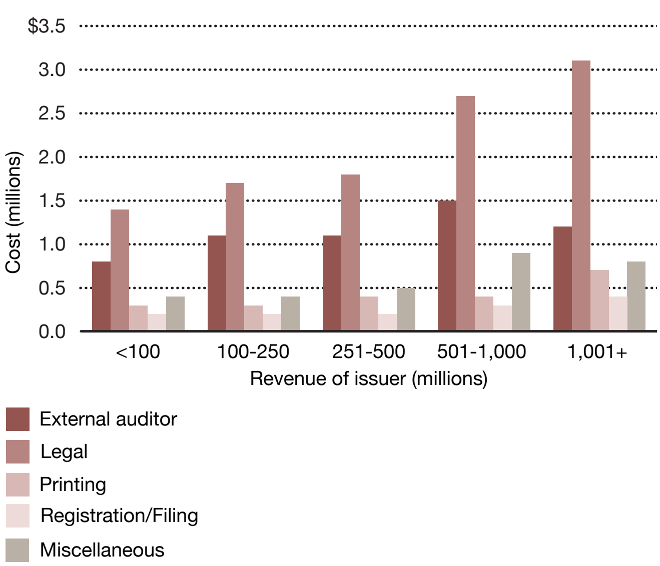
In addition to systematically preparing for an IPO through a readiness assessment, which can anticipate and prepare for surprises, companies may be able to control costs in a number of ways. There is a positive correlation between the amount of costs incurred in the IPO process and the length of time from initial filing to the effective date. A best practice is to identify an individual internally or utilize an IPO advisor that can help management as they: build the IPO plan, keep task lists, monitor progress, forecast delivery dates, identify gating issues, and keep decision making on track. Further, companies may be able to minimize accounting and legal costs by ensuring the initial filing is complete, all areas of potential SEC focus have been thoroughly prepared for in advance of the initial filing, and comments made by the SEC are then responded to in a timely manner with complete and accurate information. Many companies create unnecessary work and incur additional expenses due to insufficient responses and an inability to respond to the SEC in a timely and satisfactory manner.

A thorough IPO readiness assessment can also help prepare a budget of costs and help narrow down the range of fees as potentially troublesome issues can sometimes be identified early in the process, likely resulting in time and cost savings throughout the IPO process.

Exhibit 6
Offering costs incurred, based on revenues

(Numbers in millions, except number of IPOs)		External auditor			Legal			Printing			Registration/ filing			Miscellaneous			Underwriter discount			
Gross proceeds	**Number of IPOs**	**Range**		**Avg.**	**Range**		**Avg.**	**Range**		**Avg.**	**Range**		**Avg.**	**Range**		**Avg.**	**Range**		**Avg.**	**Avg. % of gross proceeds**
<$100	186	$0.0	$5.6	$0.8	$0.1	$5.2	$1.4	$0.0	$1.3	$0.3	$0.0	$0.4	$0.2	$ 0.0	$6.7	$0.4	$0.2	$47.7	$8.4	$11.5
100-250	93	0.2	4.4	1.2	0.6	4.2	1.8	0.1	1.2	0.3	0.0	0.5	0.2	0.0	3.6	0.4	2.1	39.5	9.8	13.7
251-500	42	0.0	5.0	1.1	0.0	7.3	1.8	0.1	0.9	0.3	0.0	0.4	0.2	0.0	2.6	0.5	2.5	42.0	14.0	17.9
501-1,000	26	0.1	4.0	1.5	0.2	7.5	2.6	0.1	0.8	0.5	0.1	0.6	0.3	0.0	3.3	0.8	4.1	65.2	19.5	25.2
1,001+	42	0.1	5.0	1.2	0.5	17.0	2.7	0.1	9.8	0.4	0.1	2.4	0.3	0.0	4.5	0.8	1.1	237.9	19.7	25.1

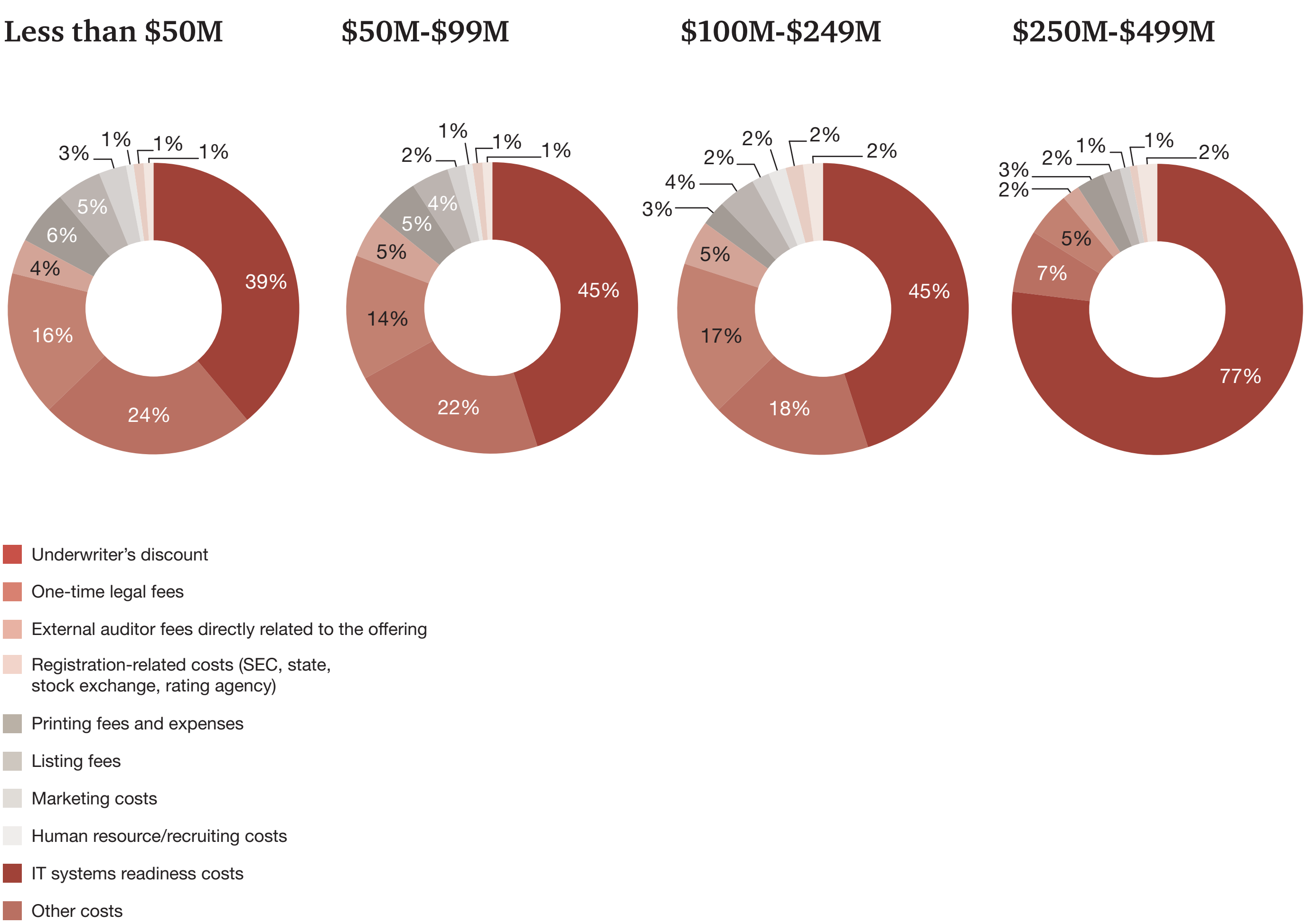
IPO costs by revenue



Underwriter discount by revenue

Exhibit 7 provides another perspective on the offering costs companies can expect to incur. One-time legal fees directly related to the process of organizing and incorporating the newly public entity can be a considerable expense, particularly for smaller companies. Based on PwC's survey of 31 recently public companies, one-time legal fees averaged nearly 25% of total costs for smaller IPO transactions of less than $50 million. For bigger transactions (from $100 million to $249 million), legal fees also comprised one of the larger costs (18%) directly related to the IPO transaction.

Exhibit 7
Proportion of one-time costs directly related to going public (based on total IPO proceeds)



A look at the incremental organizational costs incurred during the IPO process

The offering costs listed in Exhibit 7 exclude costs that are not directly attributable to the IPO, such as restructuring costs incurred to create the legal and organizational structure needed to execute the IPO. These kinds of costs are referred to as incremental organizational costs. Typically, they are non-recurring costs incurred in the months, or even years, leading up to the IPO. They can include the costs of organizing the public company, creating the registrant, and preparing for the registration process. ASC 720-15-25-1 requires these start-up activity costs, including incremental organizational costs, to be expensed as incurred. If a company cannot clearly distinguish between amounts that relate solely to the equity offering and amounts that relate to other non-offering items, then it may be necessary for the fees to be expensed in their entirety.

The following questions may be helpful when considering the potential incremental organizational costs an entity could incur during the IPO process:

- Will we use a second accounting firm to advise and assist in the IPO process and/or to assist us in the development of internal control documentation?
- Will we utilize a third party to perform valuation services to help us support a cheap stock analysis?
- What level of legal, compensation, and human resources consulting costs will we incur to create new employee benefit plans and equity-based compensation awards?
- Will we incur auditor fees related to the audit and review of financial statements to be included in our registration statement?
- Do we expect to utilize legal counsel related to the organization and incorporation of our new entity, including the drafting of bylaws and other agreements?
- Do we expect to incur IT costs or implement new systems and new reporting processes related to becoming a public company?

These incremental organizational costs vary widely and are typically based on the complexity of the transaction, the level of external support needed, and the level of the company's readiness. Total incremental organizational costs reported by recently public firms participating in PwC's survey averaged 42% of the total one-time costs, while taking their firms public.

Analyzing historical experience around incremental organizational costs is difficult because they are not required to be reported separately in registration statements. However, if these costs are significant, some companies choose to provide separate disclosures and discuss the impact of these costs on their operations within their financial statement footnotes and/or management's discussion and analysis section.

Based on public registration statements, on average companies incur underwriter fees equal to 5%-7% of gross proceeds, plus an additional $3.7 million of costs directly attributable to their IPO.

Potential impact of the JOBS Act on the going and being public process

The recent enactment of the JOBS (Jumpstart Our Business Startups) Act in April 2012 is intended in part to encourage more private companies to raise capital through the IPO process. The Act could impact the costs that companies incur in their IPOs by creating a five-year "IPO on-ramp" for emerging growth companies (EGCs), which will allow such companies more time to comply with certain disclosures and regulatory requirements. EGCs are defined as companies with less than $1 billion in annual revenues in their most recent full fiscal year and less than $1 billion in non-convertible debt issuances within the past three years, and who are not currently large accelerated filers with public floats in excess of $700 million.

Under the JOBS Act, EGCs are or will be provided a number of exemptions and deferrals in disclosure requirements. The JOBS Act allows a company that is pursuing or executing an IPO to remain an EGC for a maximum of five years, or until the company surpasses $1 billion in annual revenues or debt issuances, and is retroactive, applying to companies who have priced initial public offerings after December 8, 2011.

The JOBS Act allows for EGCs to submit two years of audited financial statements in registration statements, compared to the previous requirement of three years. Also, an EGC may submit selected financial data only for the number of years in which they have audited financial statements. For companies that decide to include only two years of financial data, management's discussion and analysis will be a comparison of the current and prior year. EGCs also are permitted to defer the adoption of new or revised public company accounting standards after April 5, 2012. In addition, the JOBS Act allows EGCs to reduce disclosure of executive compensation in certain filings with the SEC.

On the surface, these deferrals and exemptions appear to benefit EGCs, but it is unknown how the investment community will react — it is possible that the existing requirements for disclosure may continue to be required by investors. In addition, although the JOBS Act creates reduced executive compensation disclosure requirements, the benefits of a goal-aligning, incentive-based compensation program remain. Based on a review of recent filings, the SEC has required companies to include a risk factor related to the JOBS Act in their registration statement.

Costs of being public

The costs of building and maintaining a public company infrastructure

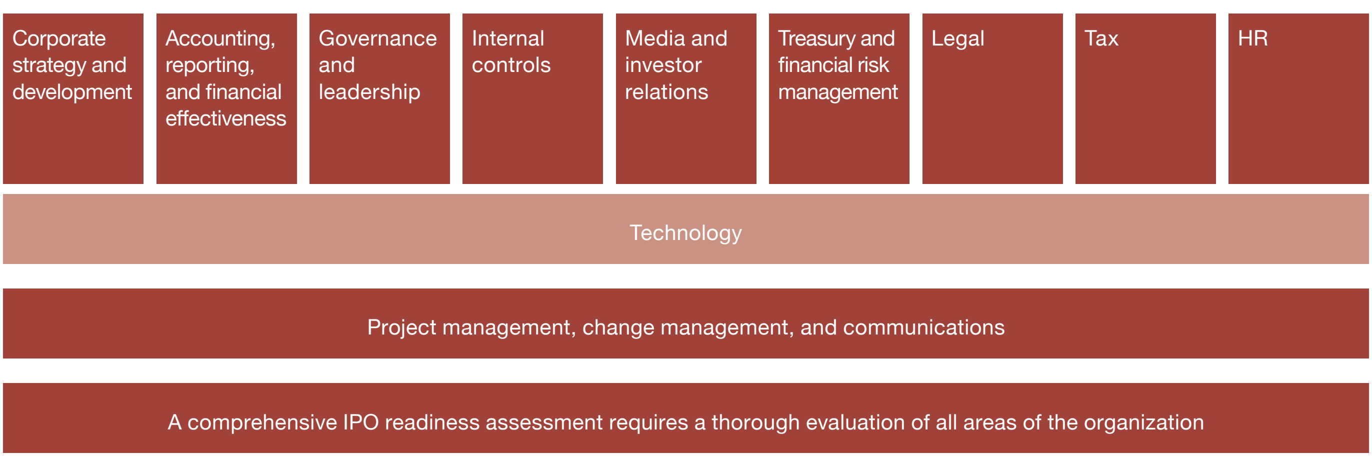
The process of undertaking an initial public offering is rigorous, time-consuming, and expensive. Many companies, having spent months exhausting their human and financial resources, view the completion of an IPO as the finish line. In reality, this is just the beginning of their new life as a public company.

As a result, in addition to the costs associated with going public — the offering and incremental organizational costs — there are significant expenses related to the being public process, which consists of developing the infrastructure to operate in a public environment. Most private companies do not have this infrastructure, and to satisfy this new level of regulatory and reporting rigor, many will incur a series of one-time and incremental ongoing costs associated with being a public company.

The following framework illustrates the areas that companies typically need to review to assess whether there are organizational and infrastructure gaps that need to be upgraded, enhanced, or filled.

In a recent PwC survey of newly public companies, 45% of firms indicated that the costs of being public exceeded their expectations.

Exhibit 8
IPO Readiness Framework



As companies think about their being public process, many choose to enhance or upgrade a wide range of different areas of their business and incur a variety of significant incremental costs related to accounting, reporting, and financial effectiveness; internal staffing needs; SEC reporting; internal audit; taxation; budgeting and forecasting; and HR and technology support.

Accounting, reporting, and financial effectiveness

Once effective, public companies are required to comply with a host of financial reporting and other requirements. The most significant change for many companies is the need to close and report publicly on their financial results on a rigorous timeline. This is a process the company will need to be fully prepared to meet; the inability to meet these requirements can shake investor confidence and potentially prohibit the company from completing capital market transactions while out of compliance. For most private companies, these are changes that take some time to implement and cannot be fixed overnight. As such, the company is well advised to ensure that it can comply with these requirements from the start.

Preparing for life as a public company should happen in parallel with the process the company undertakes for its IPO. The company should take stock of its processes and infrastructure so it can make any necessary changes as part of the IPO process. Key questions to ask include:

- Do we currently have a repeatable monthly and quarterly close process? Do we have the ability to close our books accurately each quarter, and to review and report the results to the public in accordance with SEC guidelines?
- Does our finance department have the expertise with SEC accounting and reporting requirements to allow us to comply with regulations we did not need to consider as a private company?
- Does our financial planning and analysis function have the ability to accurately forecast our results to allow for more effective interaction with the investing community and to assist in analysis of the current period results for reporting purposes?
- Does our board of directors and audit committee have the requisite experience?
- Have we established an ethics and compliance process and communicated it throughout the organization?
- Are all our processes and controls adequately documented and tested, or do we have a plan to comply with Sarbanes-Oxley and JOBS Act requirements?
- Does our technology infrastructure adequately support our compliance efforts?

On average, companies incur more than $1 million of one-time costs as a result of going public.

As a result of these considerations, there are a number of different types of costs that are incurred, both one-time and incremental ongoing costs, such as internal staffing, external resources, corporate governance, Sarbanes-Oxley, audit fees, and directors and officers insurance. Historically, the costs incurred to put in place the processes and controls required by Sarbanes-Oxley are higher during the first year than in subsequent years, after the processes and controls are more established. According to nearly half of the PwC survey participants, pre-IPO costs associated with Sarbanes- Oxley compliance (compliance with Sarbanes-Oxley as a whole, not just Section 404), ran from $100,000 to just under $500,000. An additional 13% (primarily comprised of the larger and more complex organizations) indicated that these costs exceeded $500,000. While EGCs can elect to avail themselves of the Section 404 (b) deferral provisions of the JOBS Act, CEOs and CFOs of EGCs still have to certify to the quality of the company's internal controls environment and to the financial statements in future periodic reports. Moreover, the costs to a company of a restatement can be much higher for a public company as opposed to one that is still private. As a result, EGCs should still strive to build a strong internal control environment prior to becoming a public company.

Financial reporting, regulatory compliance, and incremental auditing costs together can account for an estimated 54% of the total ongoing costs directly associated with being public, according to PwC's recent survey on benchmarking the costs of managing a public company. The survey also indicates that ongoing legal costs incurred to manage a public company account for an additional 17% of the total costs.

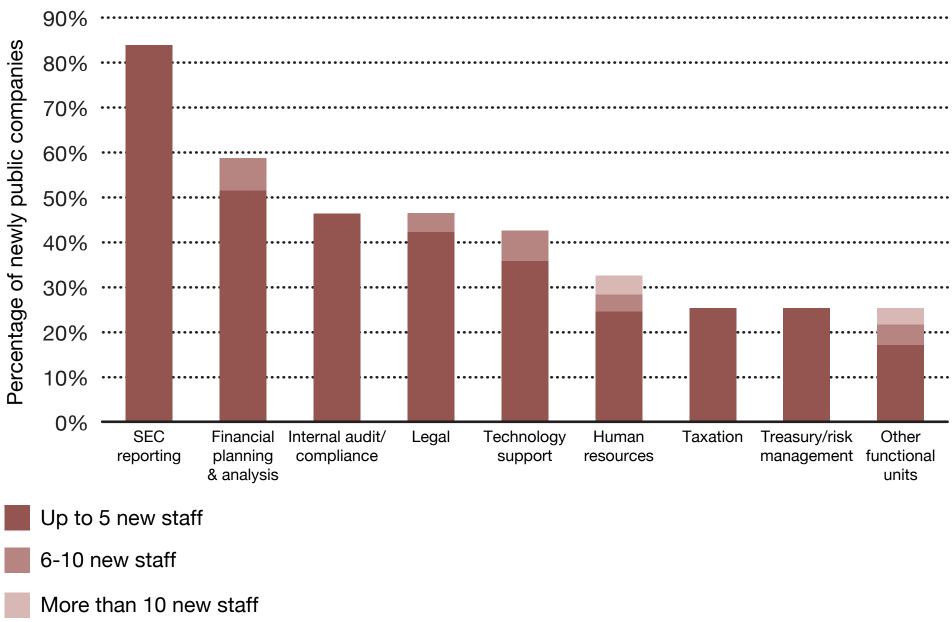
Internal staffing considerations

Public company reporting requirements often require an organization to add and retain employees who possess skill sets a private company does not have. For example, 84% of recently public firms participating in PwC's survey hired between one and five new staff specifically to increase their SEC reporting capabilities.

Additional staff requirements account for a significant portion of cost differential between public and private companies. Financial planning, internal audit and compliance, legal, and technology support are other units within public companies that often have to add staff to acquire new capabilities, according to PwC's recent survey (see Exhibit 9). Other areas where newly public companies may need to hire people include human resources, taxation, and treasury and risk management.

84% of recently public firms hired between one and five new staff specifically to increase their SEC reporting capabilities.

Exhibit 9:
Functional areas where newly public companies need to add staff



While the actual costs incurred are highly dependent on the size and complexity of the company and the expertise of its existing personnel, it is clear that the costs of these additional hires can add up quickly. According to PwC's survey, 29% of firms spent more for internal staffing needs since going public than they anticipated prior to the IPO. For 10% of surveyed firms, these costs exceeded expectations significantly. Exhibit 10 shows the additional staffing needs of public companies and the average salaries those positions command.

Exhibit 10
Salary costs for newly public companies

Staffing needs of public companies

Functional unit	Position	Salary range Low	Salary range High	Bonus, fringe benefits, and taxes	Estimated fully loaded cost
SEC reporting team	Director of financial reporting	$125	$150	$40	$ 175
	Manager of financial reporting	95	115	35	140
Taxation team	Director of taxation	135	165	60	210
	Manager of taxation	100	120	30	140
	Tax accountant	50	60	15	70
Internal audit	Director of internal audit/ compliance	125	155	40	180
	Manager of internal audit/ compliance	95	120	30	135
	Internal audit IV	75	90	20	105
	Internal audit III	65	80	20	90
	Internal audit II	50	65	10	65
	Internal audit I	45	55	10	60
Financial planning and analysis	Director of FP&A	120	145	40	175
	Manager of FP&A	90	115	30	130
Treasury and risk management	Treasurer	180	220	95	295
	Assistant treasurer	105	130	40	155
	Treasury analyst	50	60	15	70
Investor relations	Manager of investor relations	110	130	40	160

Notes:
1. All data from PwC analyses on companies with annual revenues between $500 million and $1 billion.
2. Estimated fully loaded cost determined using the midpoint of the salary range.
3. A fringe rate of 20% has been applied to all positions.
4. The above salary costs can vary significantly based on factors such as geography, industry, job description and other external factors.

Why do public companies need to hire these people? The sections below highlight the reasons why staff needs to be hired in each area to comply with SEC and other regulations and requirements. In practice, however, many private companies considering an IPO do not plan or budget for these types of costs.

SEC reporting

A typical SEC reporting team includes a director of SEC reporting and additional personnel commensurate with the size and complexity of the company and its financial reporting objectives. The SEC reporting team is responsible for ensuring that all filings made with the SEC are timely and in compliance with the SEC's rules and regulations.

Taxation

A typical taxation team includes a tax director, one or more tax managers, and additional personnel commensurate with the size and complexity of the company. The taxation group is typically responsible for ensuring compliance with all federal, state and international tax requirements in the income tax area, as well as compliance with indirect taxes including sales/use taxes, property taxes, and value added taxes.

Tax accounting and reporting will become an increasingly important and time consuming task for a public company's taxation team. Tax departments will be subject to shorter quarter and year-end close cycles. In addition they will be subject to specific interim reporting rules which govern the quarterly tax provision preparation process and more robust disclosure requirements for year-end reporting. The taxation team's controls over its tax accounting and reporting process must also comply with Section 404 of the Sarbanes-Oxley Act.

In addition, as a public company a tax department's management of its overall tax planning function will become increasingly important. Effective tax planning will drive enhanced shareholder value through management of the company's effective tax rate and the related impact on EPS.

Internal audit

Companies that list on the NYSE are required to establish an internal audit (IA) function. Companies that list on the NASDAQ are not; however, it has become a best practice and a good way to implement an appropriate internal controls environment, as well as support the required testing and Sarbanes-Oxley certification processes. In addition, IA functions can assist in dealing with the other regulatory requirements you will face as a public company.

The IA function is generally responsible for ensuring that the company's policies and procedures are implemented and executed in accordance with the company's risk management objectives. Often, IA will assist management in performing tests and other procedures designed to help the company comply with Section 404 of the Sarbanes-Oxley Act, as well as providing comfort to the CEO and CFO when they sign the 302 certification attesting to the accuracy of financial information and operating results published in periodic reports.

Many companies will look to engage external resources to help support their IA function rather than hiring additional staff. The cost to engage external resources could be higher than the cost to hire IA resources internally, but this option has several definite advantages. Utilizing external resources allows the company to scale up and scale down rapidly without having to hire or dismiss internal resources. Also, external resources may include topical specialists that can provide significant value to the IA function and be used to transfer additional knowledge to the local resources.

For many small to mid-sized companies, the IA function and compliance function may be one and the same. However, mid-sized to large companies implementing best practices, maintain separate rules and resources for the IA and compliance functions.

The accelerated financial reporting requirements and increased investor relations demands of newly public companies reinforce the need for a strong technology environment.

Financial planning and analysis (budgeting and forecasting)

Budgeting and forecasting will become an increasingly important task in the life of a public company. Research analysts rely on this information, and a public company's ability to meet its own earnings estimates and "The Street's" estimates can have a significant impact on its stock performance. Accurate budgeting and forecasting is critical for a successful IPO and for the ongoing life of a public company. Therefore, it is paramount that the company has a well-functioning financial planning and analysis (FP&A) team. The FP&A team will be responsible for developing realistic budgets and forecasts and be able to articulate why variances have occurred.

Treasury and financial risk management

A dedicated treasury and financial risk management group is also a requisite for a public company. Often, newly public companies struggle to adequately manage their liquidity, foreign currency exposure and derivatives used to hedge interest rates, and other risks to their business. An experienced treasury and financial risk management function can mitigate the growing pains that come with being a newly public company.

Human resources

Companies will likely also need to increase their human resources function as a result of becoming a public company. Many companies struggle with these increased human resources-related demands. The human resources group is typically responsible for ensuring competitive salary ranges for employees as compared to other public companies, establishing compensation policies for executives, creating new stock-based compensation and benefit plans, and working through other items associated with being a public company.

Technology support

Companies must also consider the need to increase their technology function as a result of becoming a public company. Specifically, companies must ensure that their systems and processes are documented and tested to comply with Sarbanes-Oxley requirements and that their technology infrastructure adequately supports compliance efforts. The accelerated financial reporting requirements and increased investor relations demands of newly public companies reinforce the need for a strong technology environment.

Internal staff assessment

In addition to the more specialized resources needed by a public company, more personnel across all functions of the organization may be needed to satisfy the incremental reporting and analysis requirements that come with public reporting. These additional burdens require that a company considering going public reassess its current position-specific roles and responsibilities to ensure that its staffing going forward will be adequate, both in terms of quantity and quality (skill sets and experience levels).

Board of directors

Public companies can also expect to pay director fees to independent members of its board of directors. While pay practices vary by industry and size of company, organizations generally provide packages that consist of annual retainers, additional retainers for committee or board chairman roles, and retainers for committee service. Additionally, these independent directors often receive sign-on equity grants in addition to annual equity grants. Figure 10 shows market-competitive cash compensation levels for independent directors of companies with annual revenues between $500 million and $1 billion. As illustrated in Figure 11, the average board of directors includes eight members, with an average annual retainer of approximately $45,000 per director. Audit, compensation, and governance committees generally have four members, with annual fees ranging from $2,500 to $10,000 per director. In some cases, directors begin work prior to the IPO, resulting in additional fees paid to these directors.

Exhibit 11
Board of directors fees

Board of directors fees [1]

Payment type	Number of directors receiving [3]	Amount [2]	Estimated expenses
Annual retainer	8	$45,000	$360,000
Chairman-additional retainer	1	20,000	20,000
Audit committee			
Chair	1	10,000	10,000
Member	3	4,000	12,000
Compensation committee			
Chair	1	7,500	7,500
Member	3	3,000	9,000
Governance committee			
Chair	1	5,000	5,000
Member	3	2,500	7,500
Total			$431,000

Notes:
1. All data from The Conference Board's 2011 US director compensation and board practices report for companies with annual revenues between $500 million and $1 billion.
2. The table only includes cash costs and does not include equity grants made to directors.
3. The median board includes eight independent directors.

Many companies will need to engage external resources during and after the IPO process

In addition to the significant costs required to permanently hire people with skill sets not typically found within a private company, many companies will need to engage external resources to provide technical expertise. Typical positions companies seek external advisory services include:

- Securities counsel
- Investor relations
- Accounting advisors
- Compensation advisors
- Securities counsel

During a company's IPO process, an experienced securities counsel will be heavily leveraged to provide legal advice to the company in its dealings with the underwriters and the SEC. Generally, these pre-transaction attorneys will be retained to provide ongoing services to the newly public entity, assisting them in compliance with regulatory requirements and advising the company regarding securities-related litigation. Average costs per hour charged by securities counsel can vary significantly based on the complexity of the work they are engaged to perform (i.e., transaction-based engagements may result in a significantly higher rate compared to routine Form 10-K and 10-Q filings).

Investor relations

Investor relations describes the department of a company or external group of advisors devoted to providing financial information and handling inquiries from shareholders and investors, as well as analysts and others who might be interested in a company's stock or financial stability. In many instances, a newly public company will opt to outsource all or a portion of its investor relations to a firm that specializes in such matters. A successful investor relations function is proactive and provides 'one voice' to the investment community by helping to integrate finance, marketing, public relations or financial media, and securities law compliance to enable effective communication between a company, the financial community, and other stakeholders. Its goal is to better position the company in the marketplace.

Financial reporting advisors

Although companies historically sought advice on financial reporting topics from their auditors, in the post-Sarbanes-Oxley era, many companies opt to obtain transaction support and other advisory services from a second accounting firm that is likely not restricted by SEC independence rules. For a newly public company, a financial reporting advisor can be particularly valuable in the months immediately following an IPO. A knowledgeable financial reporting advisor can advise the company as it:

- Implements the new financial reporting protocols necessary for it to meet public company reporting requirements, along with receiving ongoing technical advice on these requirements
- Adopts new accounting, reporting, and disclosure standards (or, for EGCs under the JOBS Act, advise on the choice to adopt or defer the adoption of new accounting standards)
- Trains accounting and finance staff
- Evaluates Section 404 of Sarbanes-Oxley (Note: the JOBS Act defers the requirement for auditor attestation of Section 404 (b) while the company is an EGC, but the internal control management reporting requirements of Section 404 (a) would remain intact)

Compensation advisors

Companies may benefit from the services of compensation advisors both before and after their IPO. Prior to the IPO, compensation advisors will assist private companies in establishing new annual cash incentive plans aligning pay-outs with public company performance metrics. Post IPO, compensation advisors can assist the compensation committee with governance efforts.

Meeting compliance and regulatory requirements

Corporate governance

Both the NYSE and NASDAQ have defined and published corporate governance listing standards that need to be addressed in connection with an IPO and listing of a company's equity securities. These listing standards address matters such as board composition, structure, and process — including nomination of directors, compensation practices, and similar matters — and are responsive, in part, to the Sarbanes-Oxley and Dodd-Frank Acts. The standards, however, go beyond the provisions of the Sarbanes-Oxley Act and address such matters as the establishment of a code of business conduct and ethics for employees and directors, the establishment of an internal audit function for companies listed on the NYSE and approval of related-party transactions for companies quoted on NASDAQ. A private company will likely be required to evaluate its governance structure, especially its committee charters and composition, to ensure it complies with the requirements of its chosen exchange. Companies should prepare for the time and costs required to create, implement, and maintain stricter corporate governance policies and retain high-quality members to serve on the company's committees.

Sarbanes-Oxley compliance

Although actual Sarbanes-Oxley compliance costs will vary significantly from company to company, the survey found that compliance costs for decentralized companies (i.e., those with multiple segments or operating divisions) were considerably higher than more centralized companies. Many companies will engage outside advisors to help establish a "right-sized" Sarbanes-Oxley program. Our experience in helping clients with SOX readiness projects, preparing for IPOs, and optimizing current SOX frameworks has revealed several common stumbling blocks:

- Duplicative and/or operational controls identified as key controls, increasing testing time
- Entity-level controls not effectively leveraged to minimize transaction testing
- Low-risk controls tested in the same manner as high-risk controls
- Predominant use of manual controls over financial reporting, rather than of automated application controls
- Companies not taking full advantage of the opportunity to streamline and/or enhance their business processes while implementing their SOX framework

By mapping internal controls to what's material in your financial statements and also determining where your greatest risks are, companies can often reduce the number of internal controls to maintain and test by 40% to 75%.

Audit fees

Public companies generally experience higher recurring audit fees than private companies, partly to satisfy additional regulatory requirements, including that of the PCAOB and SEC. An audit for a private company is conducted under AICPA auditing standards generally accepted in the US, whereas a public company auditor must follow the guidelines of the PCAOB, which may require additional testing and documentation. For a public company, auditors are also required to perform additional procedures related to SEC filing documentation — for example, completing reviews of the interim financial statements. When an auditor issues an opinion on a public company's financial statements, it faces additional risk, which also tends to increase audit fees.

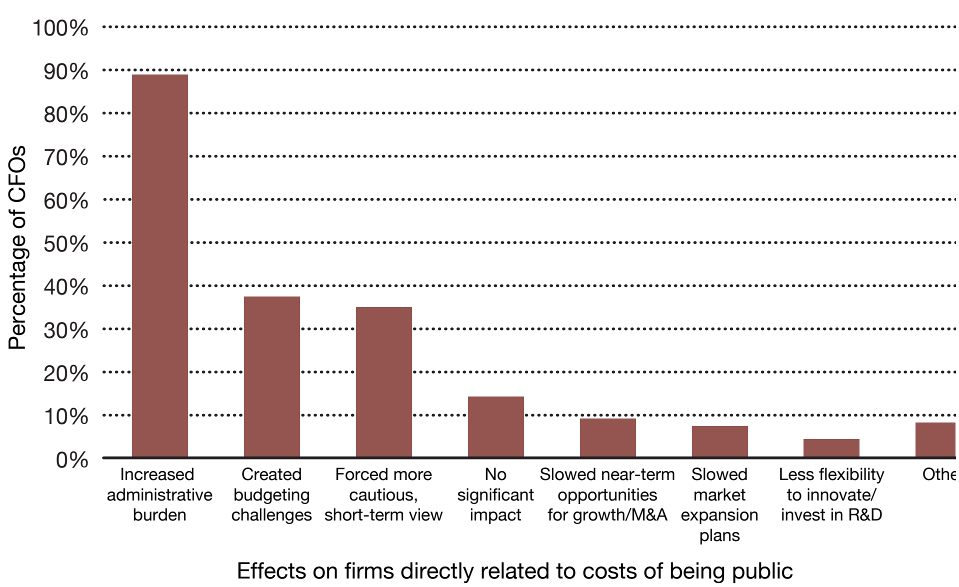
Exhibit 12
Average audit fees in 2009, 2010, and 2011 for US public companies by revenue categorization

US public companies*
Average audit fees**

Revenue group	2009	2010	2011
$1 - $100M	$203,012	$194,748	$186,201
$100M - $500M	794,465	733,680	717,379
$500M - $1B	1,343,473	1,306,900	1,263,981
$1B - $10B	3,007,453	2,910,994	2,847,914
>$10B	13,279,680	12,925,321	12,386,602

* Excludes funds, trusts, blank checks, and subsidiaries
** Based on companies that filed publicly in all years presented, excludes companies with zero and negative revenue. Audit fees consists of all fees related to audit and review services in accordance with generally accepted auditing standards. This may also include services that generally only the independent auditors reasonably can provide such as comfort letters, statutory audits, attest services, consents, and assistance with and review of documents filed with the SEC.
Source: Audit Analytics

Exhibit 13
Challenges directly related to the costs of being public



Factoring people into the being public equation

The endeavor of becoming a public company must include careful consideration of the need to develop and hire the additional staff an organization will require as a public company, not considering such an investment in personnel will likely make a private company's transition to a public entity a rocky one. It may cause unnecessary stress for current staff and management as they grapple with the challenges and competing priorities of running the business and complying with the requirements of the SEC and investing community.

Anticipating challenges related to the costs of being public

In addition to anticipating the expense that goes into taking a firm public and the ongoing costs of managing that public firm, financial managers may be unprepared for the related challenges that can result post-IPO as a direct function of these costs. The vast majority (87%) of CFOs participating in PwC's survey of recently public firms pointed to an increased administrative burden as a direct effect of the costs of being public (Exhibit 13). Greater budgeting challenges were also cited by 38% of the participating CFOs as directly linked to the extra costs of being public. Similarly, just under one-third of the surveyed CFOs felt that the extra costs of operating as a public company forced a more cautious, short-term view than had been held pre-IPO.

87% of CFOs pointed to an increased administrative burden as a direct effect of the costs of being public.

Costs of being public are difficult to predict

Unlike costs that are directly attributable to the IPO, which companies are required to disclose, there is no requirement to disclose the additional costs associated with being a public company. In fact, while many new issuers include the likelihood of additional spending as a public company in their risk factors section, only approximately 10% of filers quantify these additional expenses in their registration statements and public company filings. Additionally, as these costs can vary both in size and type, there is no uniform and consistent methodology used to estimate the costs of being a public company. The following excerpts demonstrate the variety of ways recently public companies disclose incremental organizational costs in their registration statements.

"We estimate that we will incur approximately $3.0 million of incremental costs per year associated with being a publicly-traded company; however, it is possible that our actual incremental costs of being a publicly-traded company will be higher than we currently estimate."

Rhino Resource Partners

"We estimate that we will incur between $2.0 million and $4.0 million of additional costs annually as a result of being a public company, including, among other things, the costs of auditing and reviewing our financial statements for our annual and quarterly reports under the Exchange Act, for legal fees for corporate and securities legal work to comply with rules and regulations implemented by the SEC and NYSE, for director and officer liability insurance, investor relations services, and retaining a transfer agent."

RealD Inc.

"We currently estimate the incremental recurring annual costs related to being a stand-alone public company to be approximately $38 million. The significant assumptions involved in determining the estimates of incremental recurring costs include:

- ***Additional personnel required to operate as a stand-alone public company;***
- ***Changes in compensation with respect to new and existing positions;***
- ***The level of additional assistance we will require from professional service providers;***
- ***The increase in insurance premiums and bonding costs as a stand-alone public company;***
- ***The increase in health and welcare costs associated with a larger employee base in conjunction with changes in our employee benefit plans;***
- ***The amount of additional capital expenditures for information technology infrastructure investments associated with being a stand-alone public company; and***
- ***The type and level of other costs expected to be incurred in connection with being a stand-alone public company."***

Cloud Peak Energy Inc.

Only approximately 10% of registrants disclose the additional fees they expect to incur as a public company. The level of disclosure and cost estimates vary based on size and other factors, and may include cost estimates for legal, financial reporting, finance, investor relations, and audit-related fees.

Assess the readiness of your organization for an IPO to appropriately stage the costs incurred and to minimize unexpected surprises

Many companies underestimate the time, complexity, and costs associated with transforming a private company to a public one. These costs can take many forms, from those related to engaging additional internal and external resources to the added time and expense incurred from outside legal, accounting, and advisory specialists. These costs can quickly mount and are necessary to comply with SEC-mandated regulations and the recent JOBS Act provisions. If a company fails to factor these costs into the IPO equation, it can dramatically alter once-rosy projections and negatively affect a company's valuation.

Somewhat surprisingly, only 19% of firms participating in our benchmarking costs survey had engaged a third party to perform a detailed IPO readiness assessment in advance of taking their firm public, an effort that put those companies in the best position to fully understand the costs of going public. Yet almost half of the participating firms (48%) indicated that the cost of doing an IPO exceeded their expectations, with 23% saying the costs significantly exceeded their expectations.

To avoid falling into this trap, savvy companies rely on sound project management at every stage of the IPO process and a thorough IPO readiness assessment to help them navigate the pitfalls and challenges.

Support the effort with effective project management

To coordinate the process, successful IPOs use project management resources to help management as they build the IPO plan, keep task lists, monitor progress, project delivery dates, identify gating issues, and keep decision making on track. Gating issues, in particular, can be critical to a successful launch. Failing to address the need to include a separate set of financial statements in the registration statement for a recent acquisition or the taxation effects of the post-IPO capital structure can derail the IPO process. Additionally, as companies progress through the IPO process, it can be difficult to maintain an awareness of other company initiatives that could have a significant impact on the IPO.

Perform a thorough IPO readiness assessment

As companies prepare for an IPO, an IPO readiness assessment can help identify potential big-picture issues, better cope with the challenges related to the additional costs of both going and being public, and possibly prevent embarrassing "deal-killer" surprises late in the process. The right amount of preparation also helps companies reduce costs as they establish a timetable and work plan based on the offering's strategic objectives, specific business issues, and the actual work that needs to be performed.

The IPO readiness assessment also identifies potential gaps within new processes, areas needing internal controls, and positions requiring enhanced technical accounting skills to operate as a publicly traded company. The identification of these issues early on in the process helps increase the efficiency of the IPO process. It helps companies focus on specific areas and the actions necessary to successfully complete the IPO. It is never too early to start planning.

Achieving a successful IPO requires connecting many pieces of a complex puzzle, some of which are outside of the control of company management and its stakeholders. Taking stock of the areas where management can take control and ownership of the IPO process and its aftermath is a critical first step toward capitalizing on the potential for growth and the other benefits of being public. An IPO readiness assessment, in particular, can be invaluable to holistically identify and plan for the extensive mix of direct costs associated with the IPO process and the ongoing costs that are integral to operating and maintaining a public company. Knowing these costs will increase the efficiency of the IPO and, ultimately, help stakeholders, employees, executives, and new shareholders avoid surprises and make the most of the new public company's valuation.

Today's volatile environment and fierce competition for capital compels you to be ready when the IPO window opens. An independent advisor can reduce surprises, improve efficiency, and reduce time to market. This gives you more time to focus on other crucial business decisions that will enhance market confidence in your company's management and brand equity. Leveraging the technical depth and diverse IPO experience of the right advisor can put a company in the best position for successful going public and being public transformations.

Strategy& is a global team of practical strategists committed to helping you seize essential advantage.

We do that by working alongside you to solve your toughest problems and helping you capture your greatest opportunities. These are complex and high-stakes undertakings — often game-changing transformations. We bring 100 years of strategy consulting experience and the unrivaled industry and functional capabilities of the PwC network to the task. Whether you're charting your corporate strategy, transforming a function or business unit, or building critical capabilities, we'll help you create the value you're looking for with speed, confidence, and impact.

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