Market overview

Material weakness disclosures in an IPO

Table of contents

Why disclose a material weakness?

In recent years, more companies are disclosing material weaknesses (MWs) in their Internal Control over Financial Reporting (ICFR) prior to going public, even though management may not be required to perform an evaluation of its ICFR for several years after an initial public offering (IPO). In the first half of 2021, 50% of companies going public disclosed an MW, higher than 47% in 2020, 44% in 2019 and 45% in 2018.

The wave of disclosures suggests the market increasingly expects companies to have a strong understanding of their internal controls well before their IPO. Furthermore, as we discuss later, each company filing periodic reports (e.g., Form 10-K and Form 10-Q) is required to include a certification by the company's officers as to the accuracy and fair presentation of the financial statements, as well as the adequacy of the company's ICFR and DC&P (Disclosure Controls & Procedures).

When a public company first identifies and discloses MWs in its ICFR, it may risk exposing itself to negative press, loss of investor confidence, and lower analyst ratings, which in turn, could hurt share price and the overall value of the company. Newly public companies are especially vulnerable since they have a limited history of stock market performance to guide investors.

Several factors are driving more companies to disclose MWs. They include US Securities and Exchange Commission (SEC) expectations around financial forecasts, underwriter diligence conducted as part of the going public process and the desire for full disclosure if a MW is identified, as well as increased transparency on risks investors will face. When MWs are disclosed, management is expected to take action to remediate them and to include disclosures on remediation plans.

In this report, we discuss trends in MW disclosures that can help companies prepare for an IPO.

Material weakness and internal control reporting requirements

A material weakness, as defined by the SEC, is "a deficiency, or a combination of deficiencies, in ICFR such that there is a reasonable possibility that a material misstatement of the registrant's annual or interim financial statements will not be prevented or detected on a timely basis."

Under the Sarbanes-Oxley Act (SOX), management (CEO and CFO) is required to establish, maintain and evaluate the effectiveness of ICFR. It also requires external auditors of public companies to conduct an assessment and report on the effectiveness of ICFR. The requirements and timing of compliance vary, as described in more detail later.

SOX—Key provisions

Section 302
Under Section 302, the CEO and CFO are required to certify in each annual and quarterly report that they have read the report and that report does not contain an untrue statement of material fact or omit to state a material fact. They also certify that the financial statements fairly present the company's financial condition and results of operations, and that it is their responsibility to evaluate, communicate and disclose matters relating to the company's internal controls.

Section 906
A shorter representation than the 302 certification, Section 906 requires the CEO and CFO to also certify in each annual and quarterly report that they comply with the requirements of the Exchange Act and that the information is presented fairly. Section 906 also imposes criminal penalties for certifying a misleading or fraudulent financial report. Under Section 906, penalties can be upwards of $5 million in fines and 20 years in prison.
—> Section 302 and 906 certifications are effective for companies starting with their first quarterly or annual report as a public company.

Section 404
Under Section 404, all annual financial reports must include a report stating that management is responsible for establishing and maintaining adequate ICFR and an assessment by management of the effectiveness of the internal control over financial reporting (Section 404(a)). Any material weaknesses in these controls must also be reported. In addition, in many instances, the company's external auditors must attest to the effectiveness of ICFR (Section 404(b)).
—> Sections 404(a) and 404(b) certifications are required starting with a company's second annual report after going public (with some exceptions discussed below).

With the introduction of the JOBS[1] Act in 2012, Emerging Growth Companies (EGCs), as defined under the JOBS Act, can defer the external auditor's assessment of ICFR (404(b)) for up to five years if the company maintains its EGC status[2]. Similarly, smaller reporting companies (SRCs[3]) can defer the auditor's assessment of ICFR for as long as the company remains an SRC[4]. However, regardless of whether the company qualifies as an EGC or SRC, management is responsible for establishing and maintaining adequate ICFR and is required to report on the effectiveness of ICFR starting with the second annual report after going public. Further, regardless of status, the CEO and CFO must provide the Section 302 and 906 certifications on Form 10-K or Form 10-Q starting with their first filing after going public.

Notwithstanding SOX requirements, the auditor is required to become familiar with a company's internal controls as part of its audit and may become aware of deficiencies in internal controls as a result of its auditing procedures. The auditor evaluates the severity of any deficiencies identified during the course of the audit and, upon evaluation, those considered material weaknesses or significant deficiencies are required to be communicated in writing to management and those charged with governance (generally the Board of Directors and the Audit Committee). Although the auditor is not assessing the effectiveness of the entity's ICFR, the auditor has an obligation to report to management any MWs or significant deficiencies identified during its audit.

Given all these factors, management should integrate consideration of internal controls into the company's financial processes early, to allow time to implement those controls and to adequately assess their effectiveness before going public.

Note: Companies should closely monitor their EGC status and accelerated filer status for an SRC[4] and the timing as to when they expect to lose such status as they can no longer avail themselves of the 404(b) exemption and thus, will be required to have the auditor attestation over internal controls. For example, if a company that is an EGC that went public in 2018 reported revenues of $1.2 billion for its fiscal year ended December 31, 2020, it would be obligated to comply with 404(b) requirements for the year ended December 31, 2020. Companies will need to appropriately prepare and plan for these changes to ensure compliance. Another way we commonly see companies lose their EGC or SRC status is failing the public float test—which is tested as of the last day of the company's second fiscal quarter. If the company's public float is above the prescribed levels and it becomes an accelerated or large accelerated filer, the company will be subject to the 404(b) reporting requirements as of the end of its fiscal year.

---

[1]The JOBS Act (which is short for the Jumpstart Our Business Startups Act) came into effect in April 2012 and created a number of special accommodations intended to make it easier for EGCs to complete an IPO. Such accommodations include confidential filings with the SEC, permitting two years of financial statements, and deferral of the auditor's attestation on ICFR

[2]EGCs are broadly defined as companies that meet the following criteria: (1) less than $1.07 billion in gross revenue (indexed for inflation every five years); (2) less than $1 billion in issues of non-convertible debt in a three-year period; and (3) generally less than $700 million in worldwide public float (not a large accelerated filer). An issuer that is an EGC as of the first day of its fiscal year continues to be an EGC until the earliest of: (1) the last day of the fiscal year during which it had total annual gross revenues of $1.07 billion or more;(2) the last day of the fiscal year following the fifth anniversary of the first sale of the issuer's common equity securities in an offering registered under the Securities Act of 1933 (Securities Act); (3) the date on which the issuer has issued more than $1 billion in non-convertible debt securities during the previous three-year period; or (4) the date on which the issuer becomes a large accelerated filer.

[3]SRCs are broadly defined as companies that meet the following criteria: (1) a public float of less than $250 million as of the last business day of their most recently completed second fiscal quarter; or (2) public float of less than $700 million and annual revenues of less than $100 million in the most recently completed fiscal year.

[4]SRCs may also qualify as an accelerated filer if its public float is $75 million to less than $250 million and has annual revenues of more than $100 million, in which case it would be subject to the requirements of 404(b).

Our research

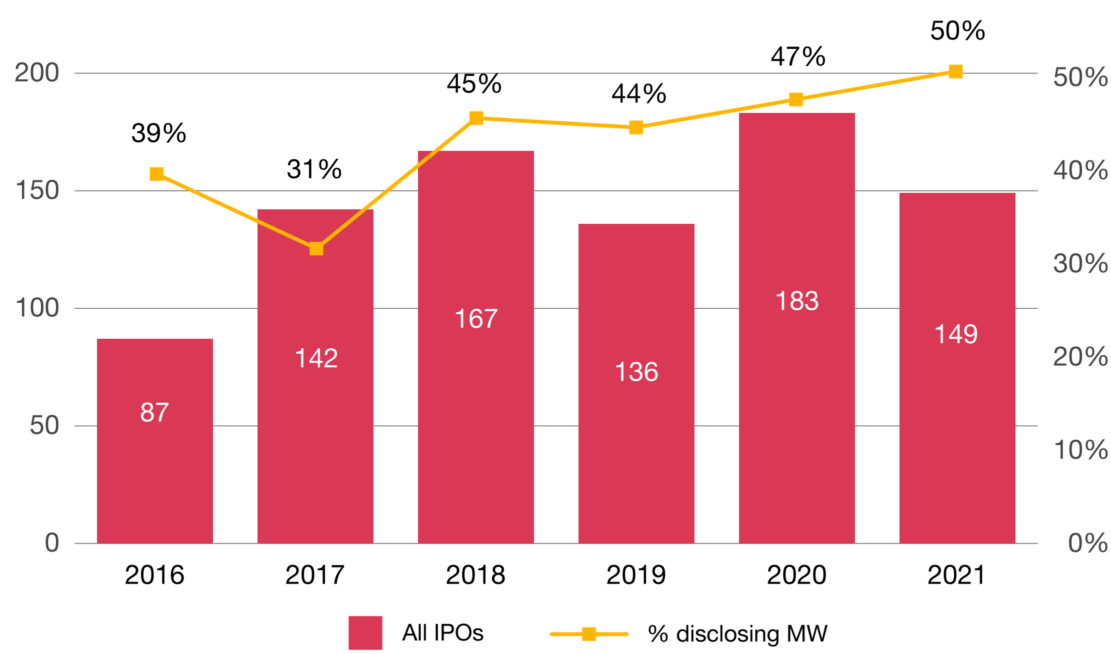
PwC researched MW disclosures in domestic and foreign issuer IPOs listed on the NYSE and NASDAQ stock exchanges between January 1, 2016 and June 30, 2021. IPOs with proceeds that are less than $25 million, best efforts offerings, oil and gas royalty trusts, business development companies, pricing on OTC Bulletin Board and OTC Pink Sheets, and special purpose acquisition companies (SPACs) are not included (see separate section on SPACs below). A foreign private issuer is defined as a non-US government, a foreign national of any foreign country or a corporation or other organization incorporated under the laws of any foreign country. All data disclosed herein is based on IPOs for the period from January 1, 2016 to June 30, 2021, unless otherwise indicated.[4]

Overall MW disclosure trends

The rate of MW disclosure in IPOs has increased significantly since 2017 (Figure 1).

Historically, IPOs with lower deal values and revenues were more likely to report MWs. However, the current trend we are observing is that the deal size and revenue do not seem to be correlated to MW disclosures. Since 2016, 44% of IPOs with a deal value[5] of $500 million or less reported MWs (these companies represented 83% of total IPOs) and 44% of IPOs with revenues of less than $500 million reported MWs (these companies represented 80% of total IPOs). IPOs with proceeds of more than $500 million have a 41% rate of MW disclosure and IPOs with revenue of more than $500 million have a 43% rate of MW disclosure (Table 1 and Table 2).

Figure 1: Percentage of IPOs disclosing MWs



[4]Material weakness disclosure is taken from the company's S-1, S-11 or F-1 registration statement. Companies undergoing IPOs may have disclosed their material weaknesses outside the year of eventual pricing; however, we are using the pricing date for the purposes of calculating year-over-year percentages.

[5]Deal value is defined as total proceeds raised in the offering.

Table 1: Percentage of IPOs with MW by deal value

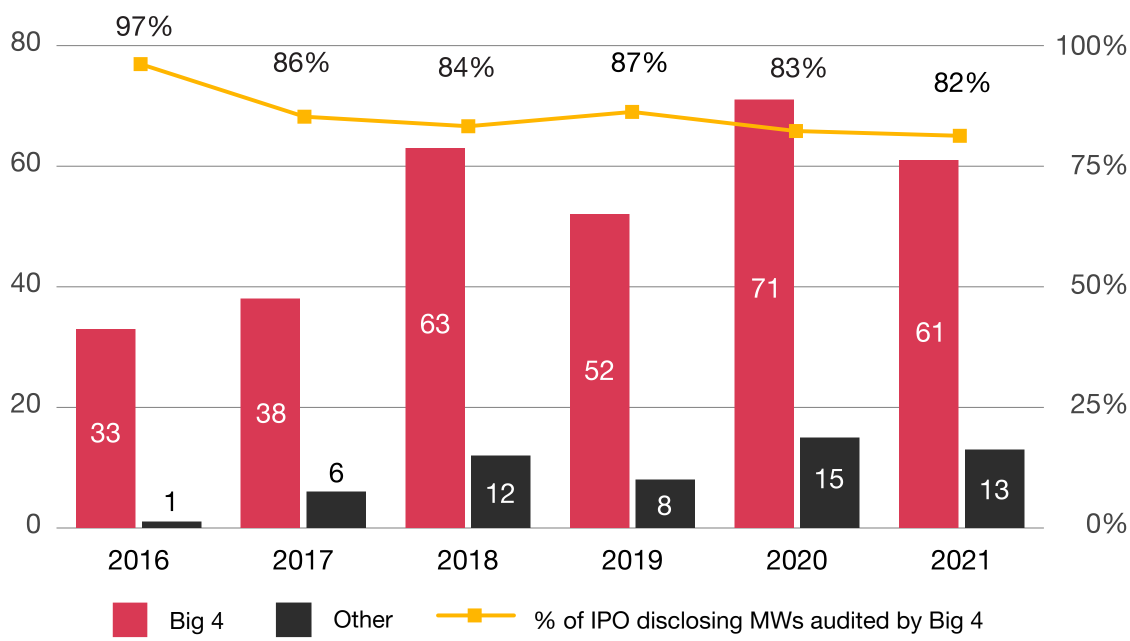
IPOs by deal value	≤$500m	>$500m	Total
% of IPOs w/MW by deal value	44%	41%	43%
% of total IPOs	83%	17%	100%

Table 2: Percentage of IPOs with MW by last twelve months (LTM) revenue at IPOvalue

IPO by LTM revenue at IPO	≤$500m	$500m–$1b	>$1b	Total
% of IPOs w/MW by deal value	44%	43%	40%	43%
% of total IPOs	80%	9%	11%	100%

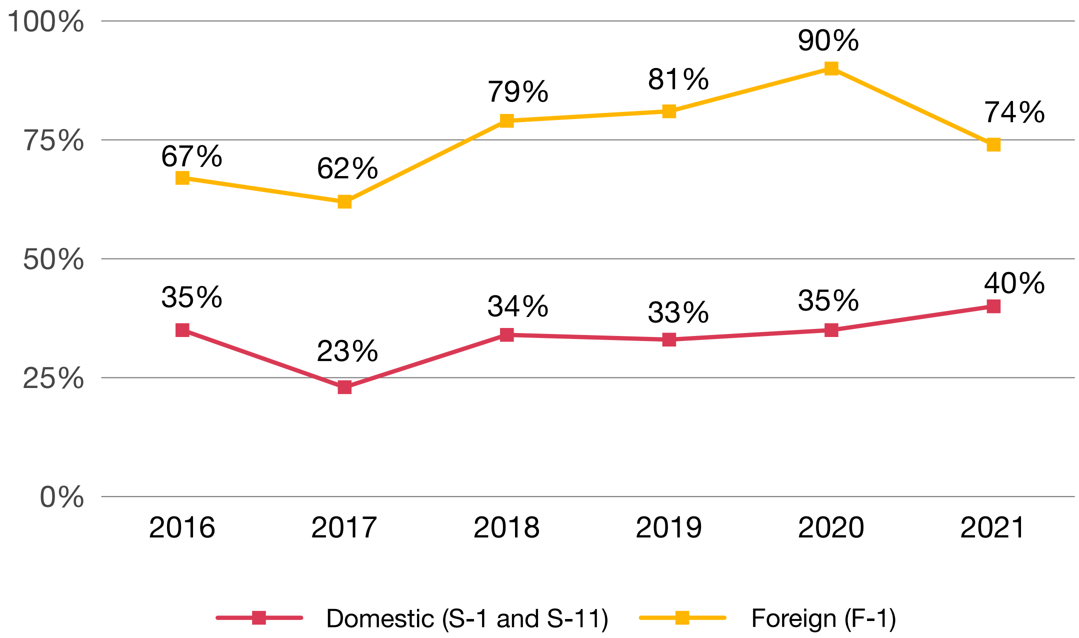
Of the IPOs that disclosed a MW since 2016, 85% were audited by a Big 4 accounting firm. This trend has remained relatively consistent year over year since 2017, with a slight decline in 2020 and 2021 in which 83% and 82%, respectively, were audited by a Big 4 accounting firm (Figure 2).

Figure 2: Auditors of IPOs disclosing MWs



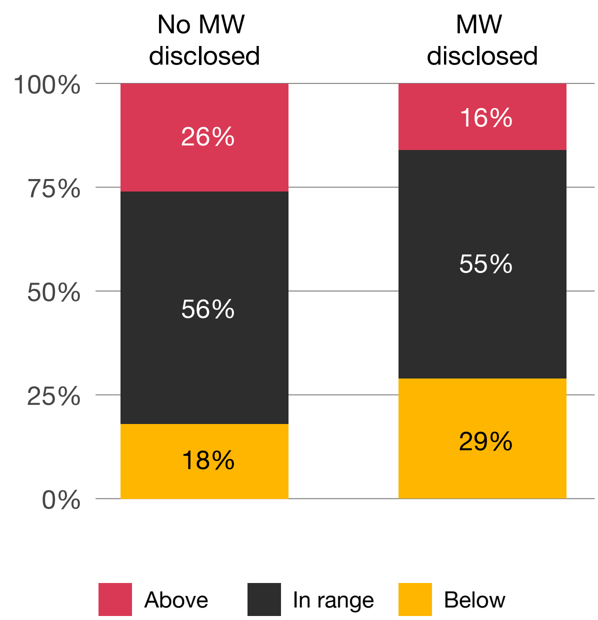
Analyzing the data based on issuer type, foreign private issuers have a significantly higher rate of MW disclosure compared with domestic issuers, which is likely driven by differences from their local rules and regulations to the scrutiny of the US reporting environment and insufficient training of personnel to operate in a US regulatory environment. On average, 77% of foreign private issuers disclosed MWs in their IPOs compared with 33% of domestic issuers (Figure 3). Since 2016, domestic issuers (which represent 81% of total IPOs) disclosing a MW have been generally consistent, with a slight decrease in 2017. However, foreign private issuers (which represent 19% of total IPOs) disclosing MWs have been increasing since 2017—only 62% of foreign issuers disclosed MWs in 2017 but 90% of foreign issuers disclosed MWs in 2020 and 74% in 2021. Notably, 65% of foreign issuers disclosing an MW list China (which represents 57% of total foreign IPOs) as their country of origin.

Figure 3: Percentage of IPOs disclosing MWs by issuer type



We also analyzed the impact of MW disclosures in a registration statement on the IPO share price relative to the range that was included in the company's registration statement used during its roadshow. The analysis shows slight differences in the ratio of companies pricing above, below or within the range for companies who did or did not disclose MWs in their registration statement (Figure 4). However, it can not be proven that MWs have a direct impact on the share price, as investors would consider all disclosed information in their initial determination of the share price and the range included in the registration statement prior to the IPO.

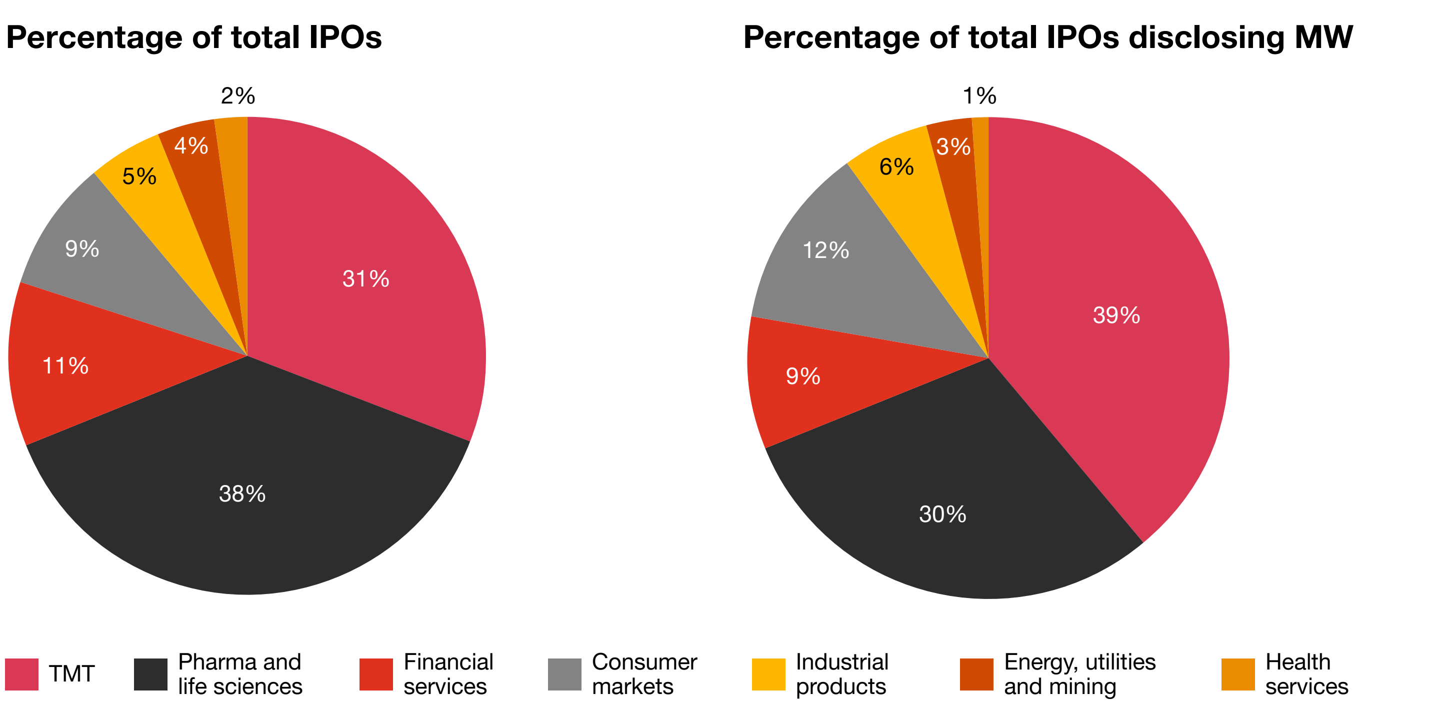
Figure 4: Impact of MW disclosure on IPO price versus share price range



Finally, analyzing data at a sector level reveals distinct trends in the rate of MW disclosure in certain sectors. Figure 5 depicts (a) the percentage of total IPOs attributable to a given sector and (b) the percentage of total IPOs reporting a MW attributable to a particular sector.

Technology, media and telecommunications (TMT) and pharma and life science sectors have the highest percentage of total IPOs disclosing MWs, with 39% and 30%, respectively. Given the volume of IPOs in these sectors, those numbers are not unexpected (Figure 5— Percentage of total IPOs). The higher rate of MWs in these sectors may be due to the complexity and volume of transactions, multinational operations and less regulation, relative to other sectors, prior to going public. For further analysis, refer to the Sector Overview section below.

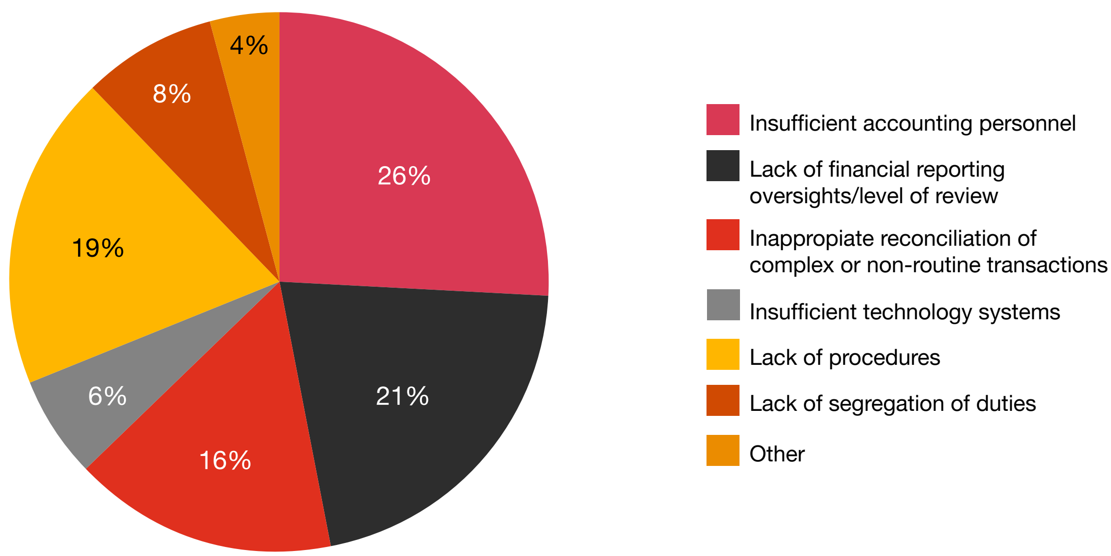
Figure 5: IPO MW disclosures by sector



Types of MWs and remediation plans

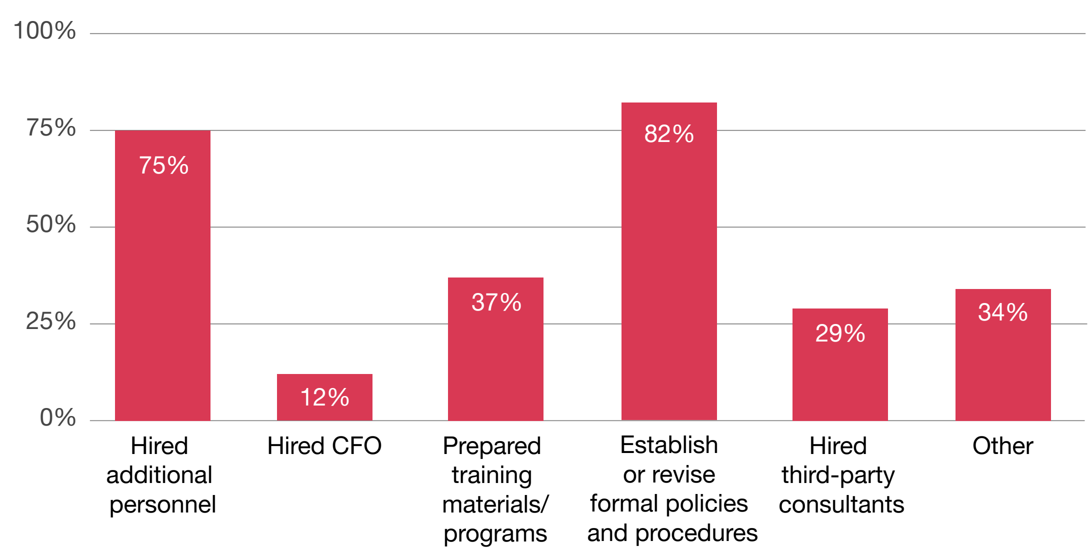
Of the companies that reported MWs, 45% reported two or more MWs with some companies reporting up to seven. The most common MWs reported (Figure 6) relate to insufficient accounting personnel (26% of total MWs), lack of financial reporting oversight and review processes (21%) and lack of appropriate procedures (19%). The types of MWs in pre-IPO companies is not unexpected, considering these companies typically have fewer resources and a leaner organization, which can result in weaknesses related to inadequate personnel, oversight and level of review. Companies that have been public longer, often identify MWs as a result of a specific issue or transaction, given the more mature and built-up functions supporting the organization. When companies disclosed MWs, they included a risk factor disclosure in the registration statement and the majority of these companies included additional disclosures in management discussion and analysis (MD&A).

Figure 6: Breakdown of MWs disclosed by type



98% of companies disclosing MWs included remediation plans in their registration statement, with many companies disclosing more than one solution to remedy their MWs. Most commonly, companies sought to remedy their MWs by establishing or revising formal policies and procedures (82%) or by hiring additional personnel (75%). Other remediation plans include hiring a CFO, preparing training materials and hiring third-party advisors. Figure 7 shows remediation solutions disclosed as a percentage of total IPOs with MWs.

Figure 7: Remediation solutions as a percentage of total IPOs with MWs

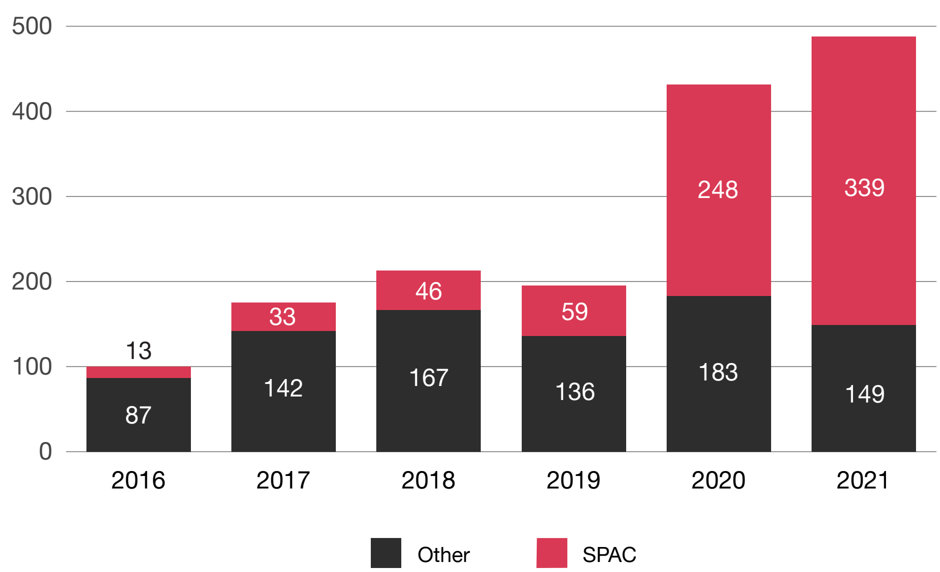


SPACs and MW disclosure

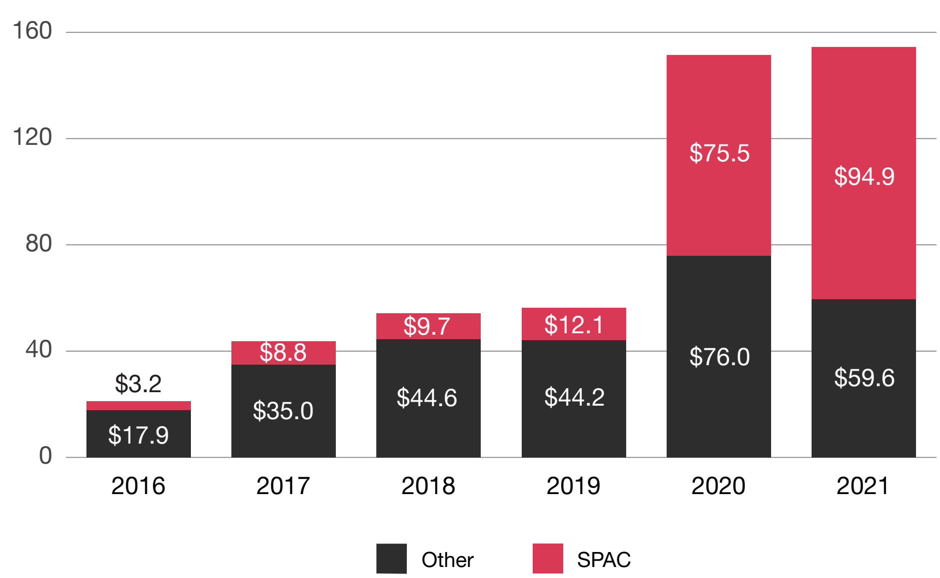
As noted earlier, SPACs were not included in the overall IPO market and MW analysis and discussion given the unique nature of a SPAC. A SPAC is a shell company formed to raise capital in an IPO in order to use the proceeds to acquire one or more businesses by a specified deadline (generally within 24 months of the IPO). A SPAC goes through the typical IPO process of filing a Form S-1 registration statement with the SEC, clearing SEC comments and undertaking a roadshow followed by a firm commitment underwriting. The IPO proceeds are then held in a trust account which will be released to fund a business acquisition if approved by the shareholders. The process to gain shareholder approval is generally through the SPAC's filing of a proxy statement (or a joint registration and proxy statement on Form S-4 if it intends to register new securities to be issued in connection with the merger), which requires it to include financial statements of the target. Once the merger is consummated, the SPAC and the target business combine into a publicly traded operating company.

Viewed as an alternative to a traditional IPO, SPAC IPOs have increased significantly over the last few years, making up approximately 69% of US IPOs in the first half of 2021 and 61% of the proceeds in that time period.

Total SPAC deal volume as compared to the overall IPO market by year

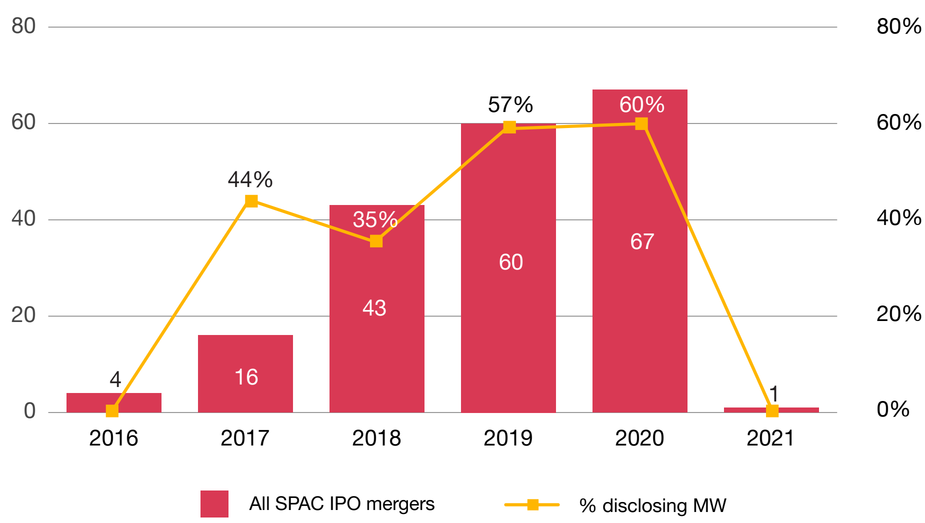


Total SPAC deal value as compared to overall IPO market by year (in billions)



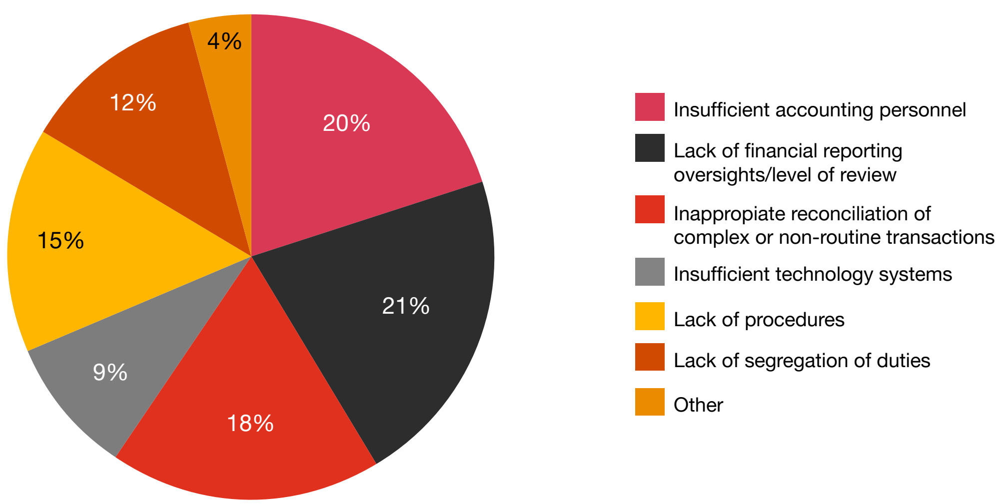
We separately analyzed MW trends in SPACs before and after mergers. Our research shows that there were no MWs disclosed in SPAC IPOs before mergers, which is not surprising given that SPACs are shell companies with limited transactions. We then reviewed the filing for the merger (which can take place up to 24 months after the effective date of the IPO), which includes the target company financial information, and noted an average of 50% of the filings disclosed an MW. The table below shows the total SPAC mergers that were completed in a given year (based on the Schedule 14A/Form S-4 filing), as well as SPAC mergers that disclosed an MW.

Percentage of SPAC IPO mergers disclosing MWs



The most common MWs reported relate to lack of financial reporting overview/level of review processes (21%), insufficient accounting personnel (20%) and Inappropriate reconciliation of complex or non-routine transactions (18%), which is consistent with the themes across the broader IPO markets. Most SPACs sought to remedy their MWs by establishing or revising formal policies and procedures (27%) or hiring additional personnel (25%).

Breakdown of SPAC MWs disclosed by type



[6] Material weakness disclosures in SPACs after the merger are taken from Schedule 14A/Form S-4 filed with the SEC. Material weaknesses disclosures in SPACs before merger were taken from S-1..

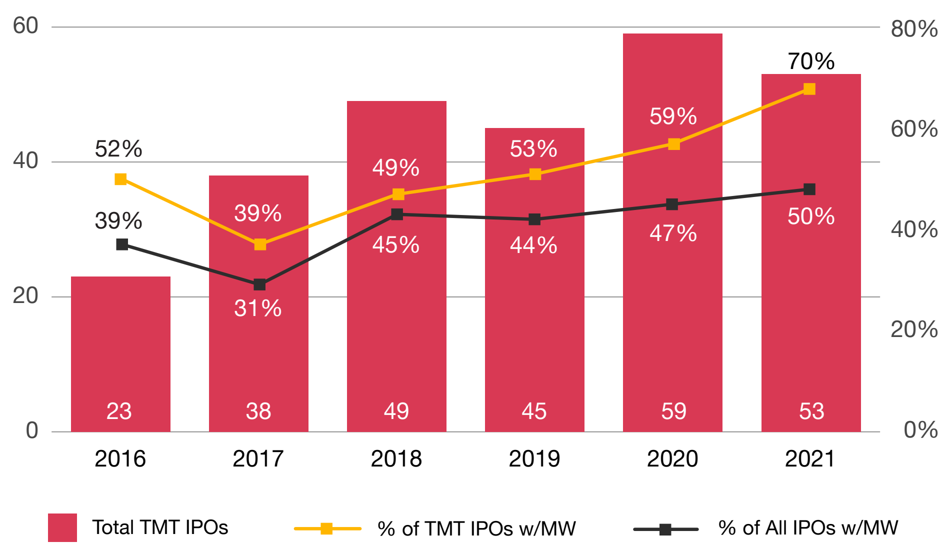
Sector overview

Technology, media and telecommunications

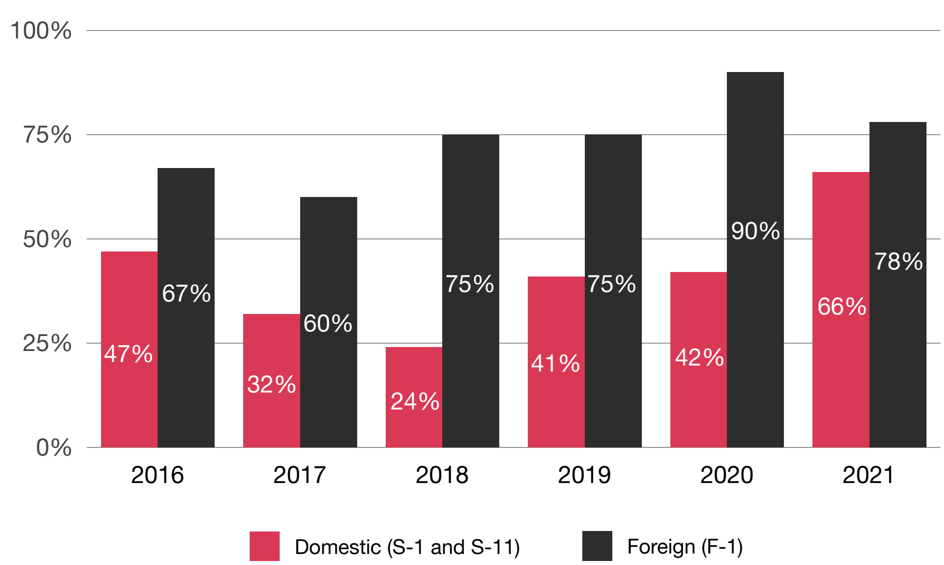
In the TMT sector, an average of 55% of the companies that went public disclosed at least one MW, higher than the average of 43% across all sectors. Of the companies disclosing an MW, 77% of foreign issuer IPOs in the TMT sector disclosed MWs (foreign issuers represent 36% of total TMT IPOs) and 43% of domestic issuers disclosed MWs. Since 2016, 59% of TMT IPOs with a deal value of $500 million or less reported MWs (these companies represented 73% of total TMT IPOs) and 56% of TMT IPOs with revenues of less than $500 million reported MWs (these companies represented 77% of total TMT IPOs).

The TMT sector IPOs are led by software, enterprise cloud and e-commerce companies where investors look to capitalize on returns from fast-moving, high-growth businesses. These companies tend to be relatively smaller in size, less mature and in an early stage of development, which could explain why the TMT sector has more companies disclosing MWs than other sectors.

TMT IPOs and MW disclosures



Percentage of TMT IPOs by issuer type disclosing MW

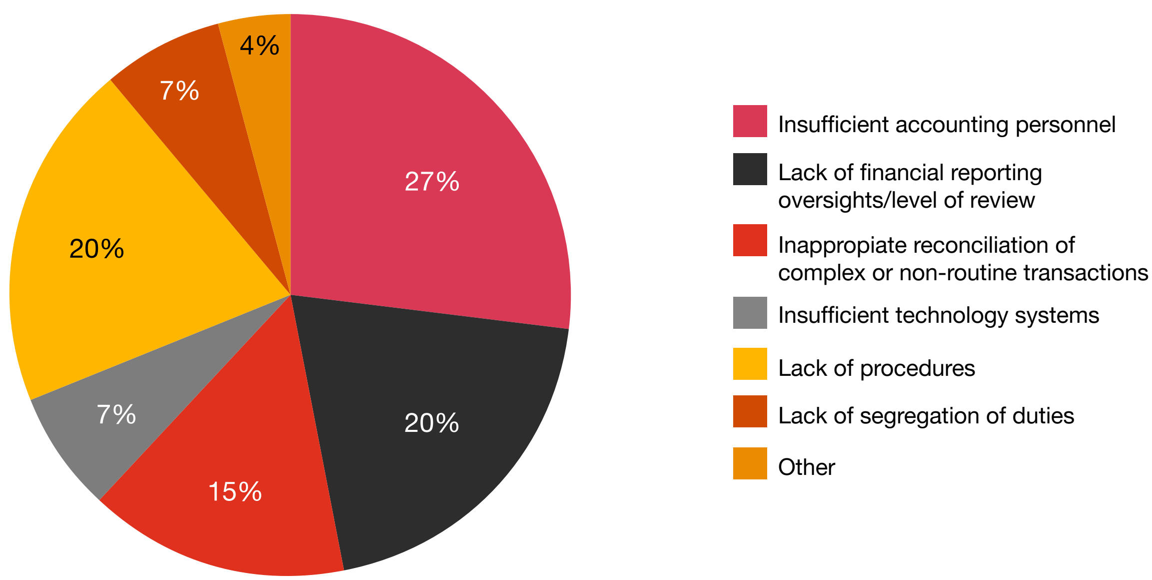


The following table shows the percentage of companies disclosing an MW within each revenue category and percentage of companies disclosing an MW within each deal size category.

IPOs with MW by LTM revenues	≤$500m	$500m–$1b	>$1b	Total
TMT	56%	58%	42%	55%
All IPOs	44%	43%	40%	43%

IPO with MW by deal value	≤$500m	>$500m	Total
TMT	59%	45%	55%
All IPOs	44%	41%	43%

TMT MWs by type

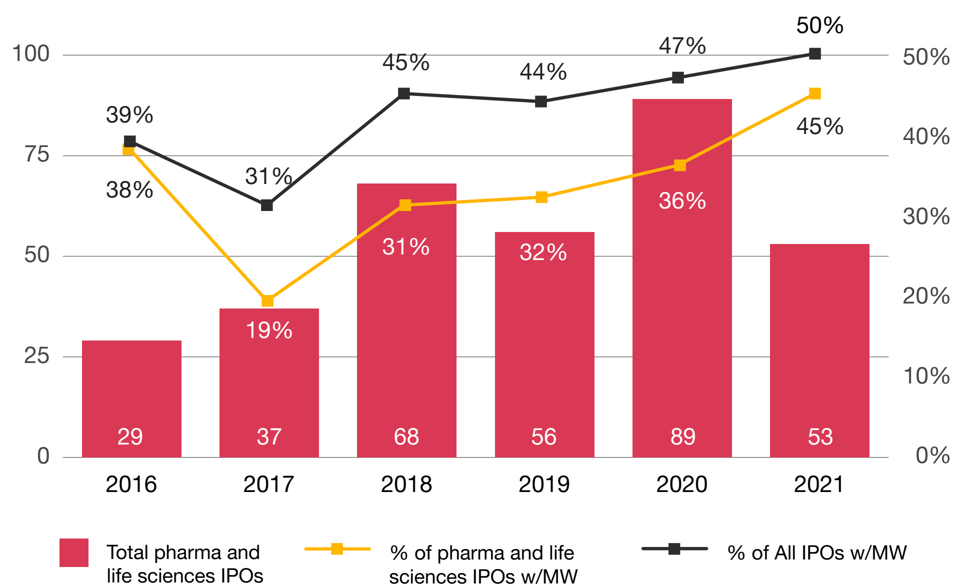


Pharmaceuticals and life sciences

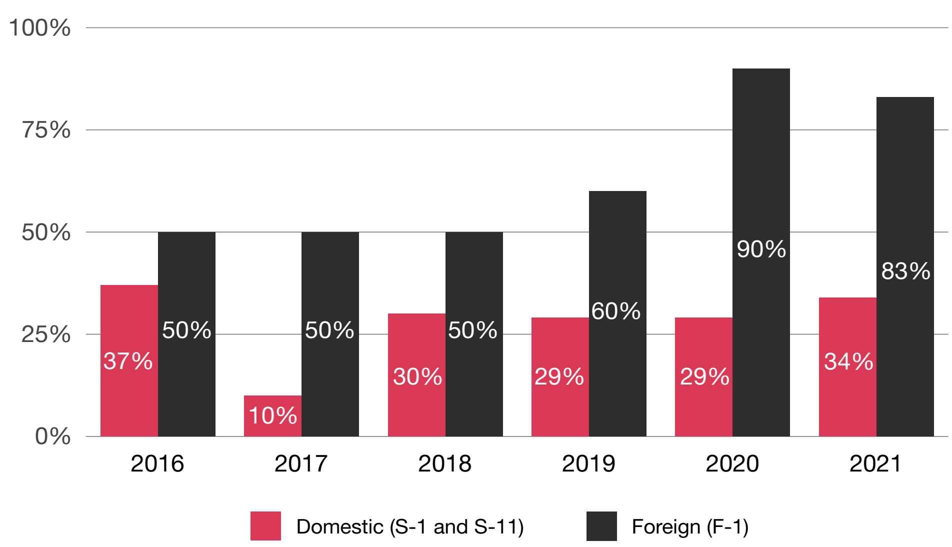
In the pharma and life sciences sector, an average of 34% of the companies that went public disclosed at least one MW, below the 43% average of companies disclosing MWs across all sectors. Of the companies disclosing an MW, 71% of foreign issuers IPOs disclosed MWs (these companies represent 12% of total pharma and life sciences IPOs) and 29% of domestic issuers disclosed MWs. Since 2016, 35% of pharma and life sciences IPOs with a deal value of $500 million or less reported MWs (these companies represented 96% of total pharma and life sciences IPOs) and 35% of Pharma & Life Sciences IPOs with revenues of less than $500 million reported MWs (these companies represented 98% of total Pharma & Life Sciences IPOs in that sector).

Although companies disclosing MWs in this sector increased significantly since starting in 2018, the overall percentage is less than other sectors. In part, this could be due to the high volume of IPOs in this sector as compared to other sectors (332 of 864 IPOs since 2016, or 38% of all IPOs). In the last few years, the pharma and life science sector has been dominated by biotech companies due to increased venture capital funding (and related exits), a rise in genomic medicine, an increase in platform vs single product companies, and increased insider participation. These companies, prior to an IPO, are generally in a very early stage of development, unprofitable or without revenue. While their main focus is on developing a viable product and less on compliance, their overall business tends to be less complex relative to other sectors which may explain why the sector on average has fewer MWs as compared to the overall IPO markets and other sectors.

Pharma and life sciences IPOs and MW disclosures



Percentage of pharma and life sciences IPOs by issuer type disclosing MW

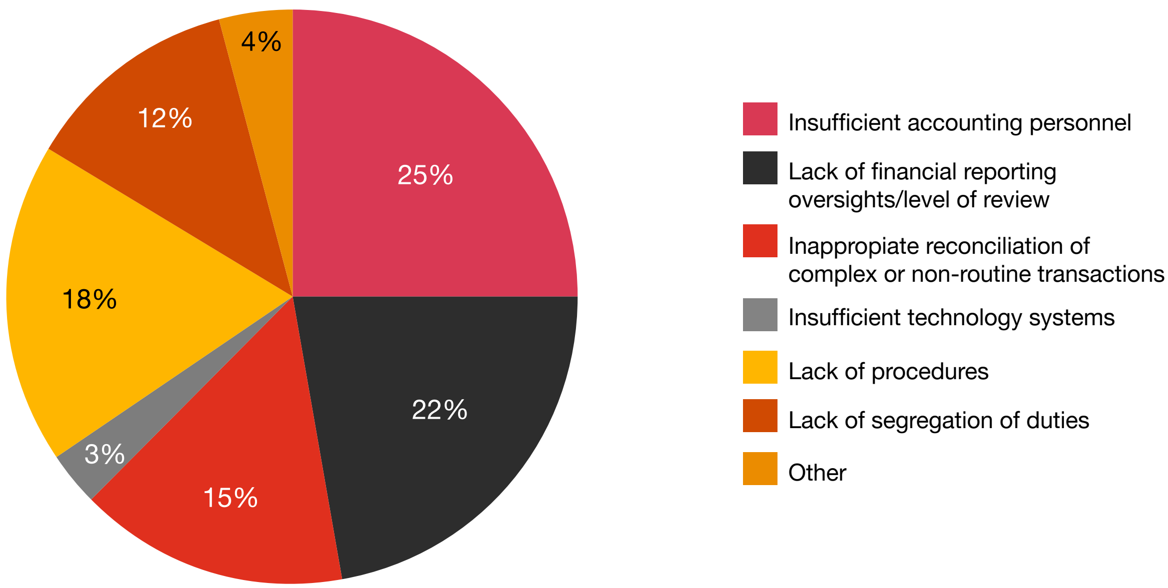


The following table shows the percentage of companies disclosing an MW within each revenue category and percentage of companies disclosing an MW within each deal size category.

IPOs with MW by LTM revenues	≤$500m	$500m–$1b	>$1b	Total
Pharma and life services	35%	0%	20%	34%
All IPOs	44%	43%	40%	43%

IPO with MW by deal value	≤$500m	>$500m	Total
Pharma and life sciences	35%	8%	34%
All IPOs	44%	41%	43%

Pharma and life sciences MW by type

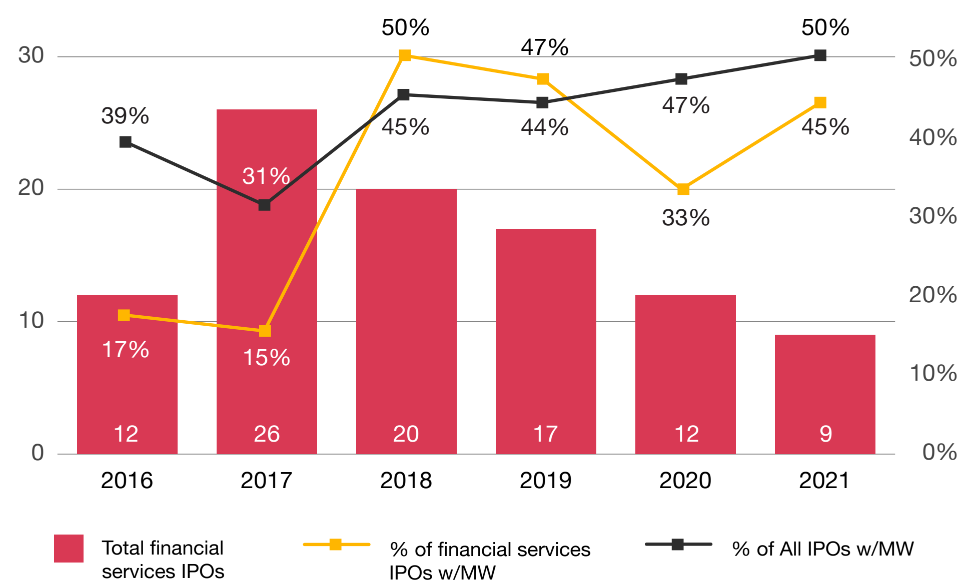


Financial services

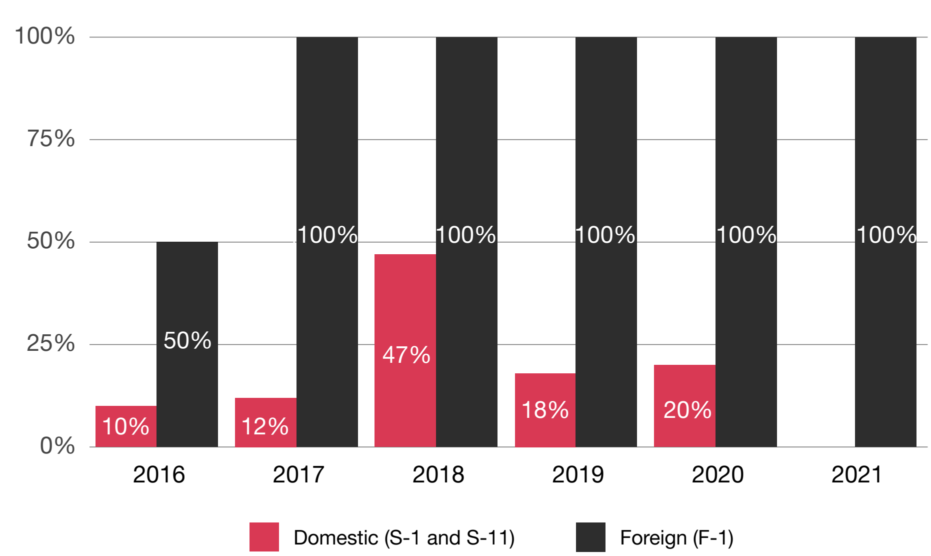
In the financial services sector, an average of 33% of the companies that went public disclosed at least one MW, lower than the 43% average of companies disclosing MWs overall. However, since 2018, there has been a significant increase in financial services IPOs where at least one MW was disclosed. Of the companies disclosing an MW, an average of 94% of foreign issuer IPOs disclosed MWs (foreign issuers represent 17% of total financial services IPOs) compared with an average of 21% of domestic issuers. Since 2016, 31% of financial services IPOs with a deal value of $500 million or less reported MWs (these companies represented 86% of total financial services IPOs) and 36% of financial services IPOs with revenues of less than $500 million reported MWs (these companies represented 79% of total financial services IPOs).

The increase in percentage of companies disclosing an MW in the last few years could be attributable in part to a decrease in the number of IPOs, as well as to an increase in non-routine complex transactions. The leading MW disclosed in this sector is lack of reconciliation of complex and non-routine transactions.

Financial services IPOs and MW disclosures



Percentage of financial services IPOs by issuer type disclosing MW

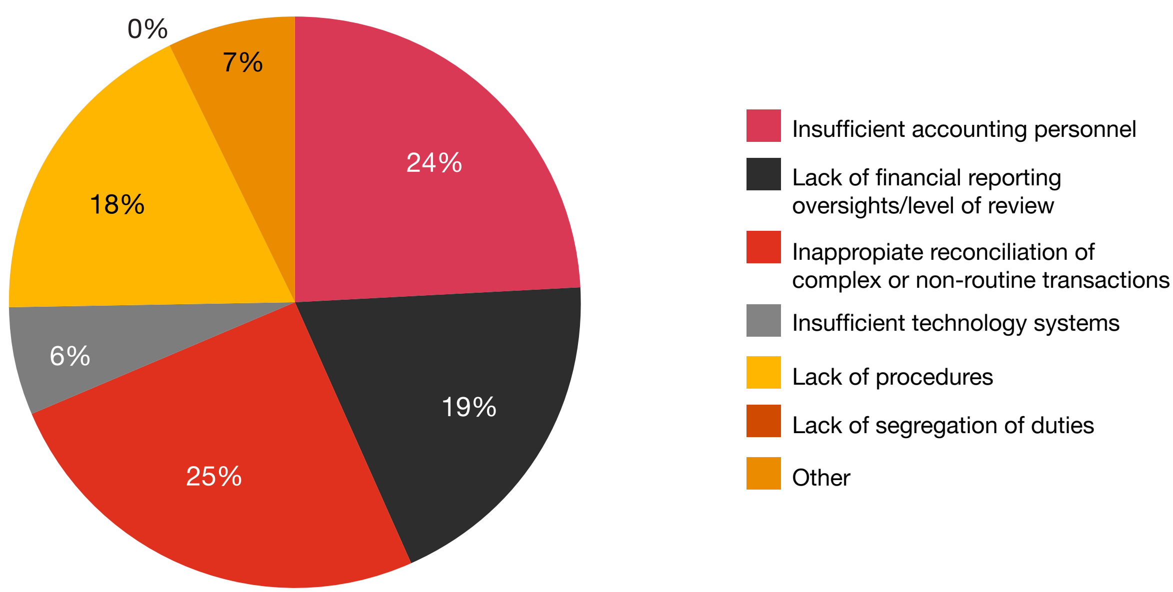


The following table shows the percentage of companies disclosing an MW within each revenue category and percentage of companies disclosing an MW within each deal size category.

IPOs with MW by LTM revenues	≤$500m	$500m–$1b	>$1b	Total
Financial services	36%	10%	40%	33%
All IPOs	44%	43%	40%	43%

IPO with MW by deal value	≤$500m	>$500m	Total
Financial services	31%	46%	33%
All IPOs	44%	41%	43%

Financial services MWs by type

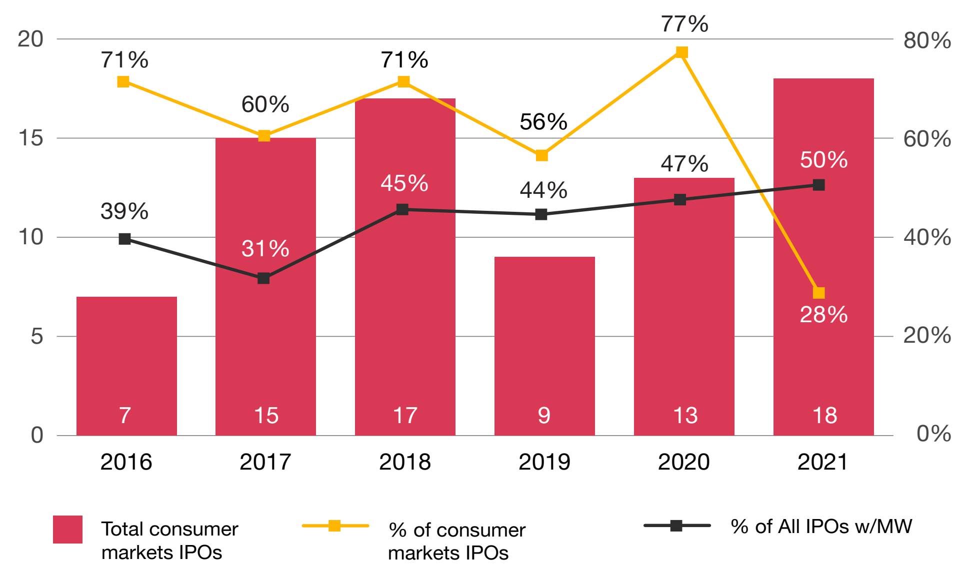


Consumer markets

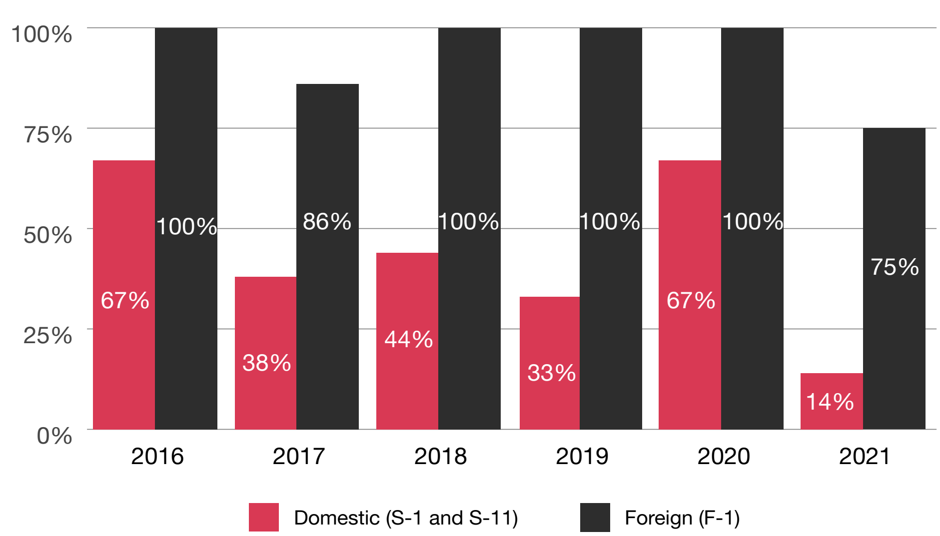
In the consumer market sector, an average of 58% of the companies that went public disclosed at least one MW, significantly above the 43% average of companies disclosing MWs across all sectors. Of the companies disclosing an MW, an average of 93% of foreign issuers IPOs disclosed MWs (foreign issuers represent 34% of total consumer market IPOs) and an average of 40% of domestic issuers disclosed MWs. Since 2016, 63% of consumer market IPOs with a deal value of $500 million or less reported MWs (these companies represented 72% of total consumer market IPOs) and 65% of consumer market IPOs with revenues of less than $500 million reported MWs (these companies represented 51% of total consumer market IPOs).

This sector's higher percentage of companies reporting an MW could be attributed in part to the high number of transactions impacted by new accounting standards as well as to the high number of foreign-issuer IPOs in this sector. The consumer markets sector IPOs increased in 2017 and 2018 due to education companies (primarily from China), which represented 33% and 24% of all sector IPOs in 2017 and 2018, respectively.

Consumer markets IPOs and MW disclosures



Percentage of consumer markets IPOs by issuer type disclosing MW

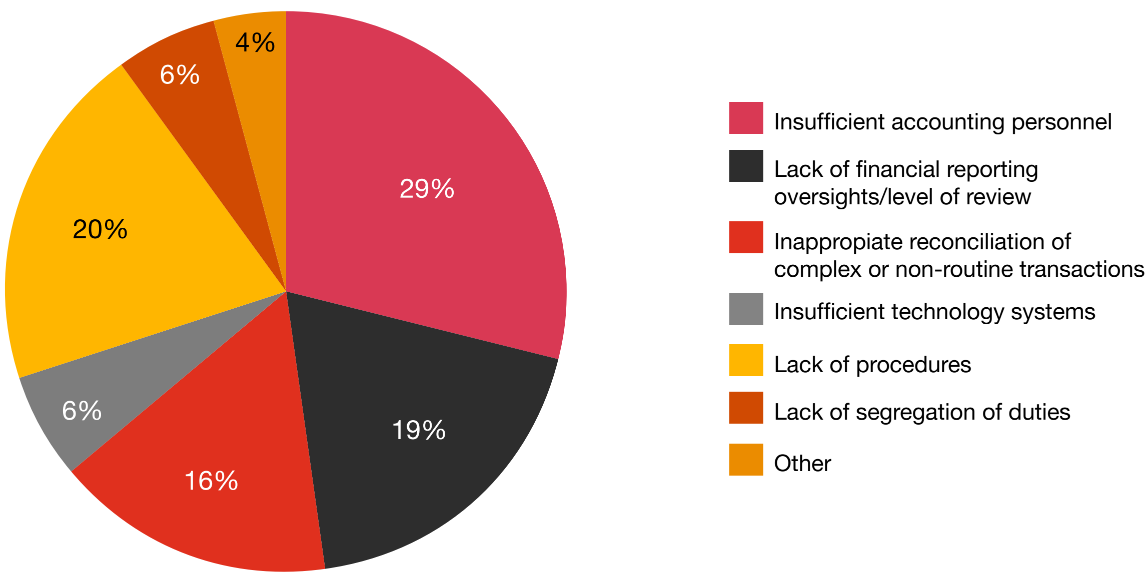


The following table shows the percentage of companies disclosing an MW within each revenue category and percentage of companies disclosing an MW within each deal size category.

IPOs with MW by LTM revenues	≤$500m	$500m–$1b	>$1b	Total
Consumer markets	65%	58%	48%	58%
All IPOs	44%	43%	40%	43%

IPO with MW by deal value	≤$500m	>$500m	Total
Consumer markets	63%	45%	58%
All IPOs	44%	41%	43%

Consumer markets MWs by type

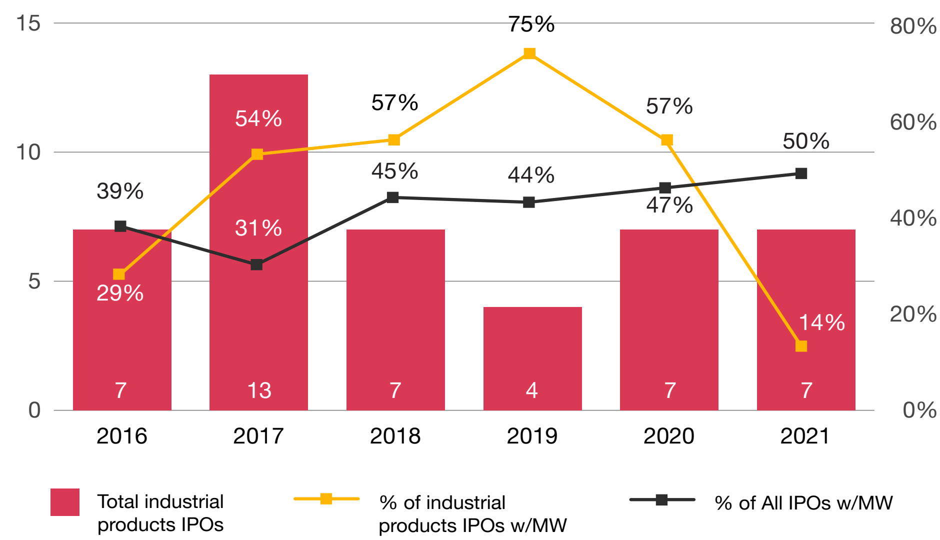


Industrial products

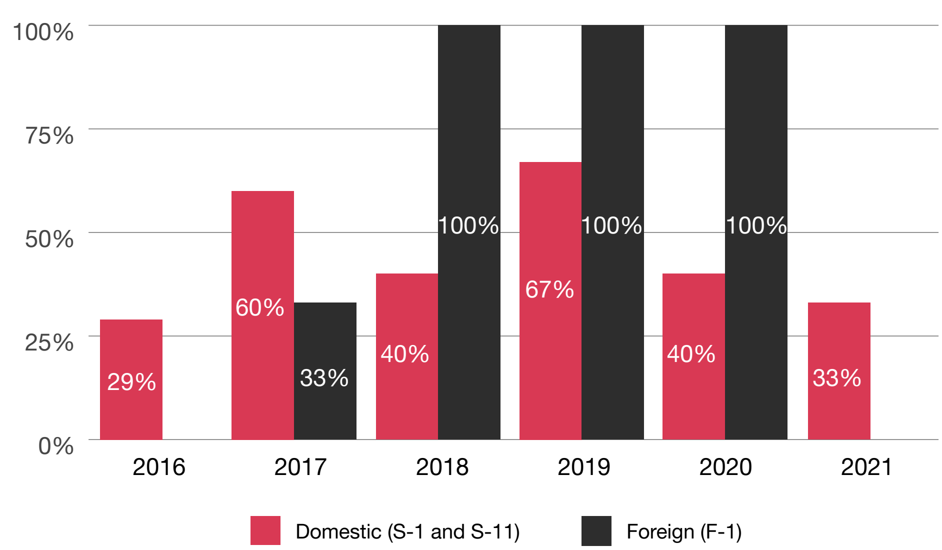
In the industrial products sector, an average of 47% of the companies that went public disclosed at least one MW, slightly above the 43% average of companies disclosing MWs overall. Of the companies disclosing an MW, an average of 50% of foreign-issuer IPOs disclosed MWs (foreign issuers represent 27% of total industrial products IPOs) compared with an average of 45% of domestic issuers disclosing MWs. Since 2016, 45% of industrial products IPOs with a deal value of $500 million or less reported MWs (these companies represented 64% of total industrial products IPOs) and 61% of industrial products IPOs with revenues of less than $500 million reported MWs (these companies represented 40% of total industrial products IPOs).

The industrial products sector had a significant increase in companies disclosing MWs, from 29% in 2016 to 75% in 2019 and a significant decrease in 2020 and 2021with only 57% and 14%, respectively, of companies disclosing MWs. From the companies disclosing an MW, all foreign-issuer IPOs disclosed MWs in 2018, 2019 and 2020. The fluctuations in the number of companies disclosing MWs could be attributable to the relatively smaller volume of IPOs in this sector (the industrial products sector accounted for 45 IPOs out of 864 total IPOs since 2016, which represent only 5% of all IPOs).

Industrial products IPOs and MW disclosures



Percentage of industrial products IPOs by issuer type disclosing MW

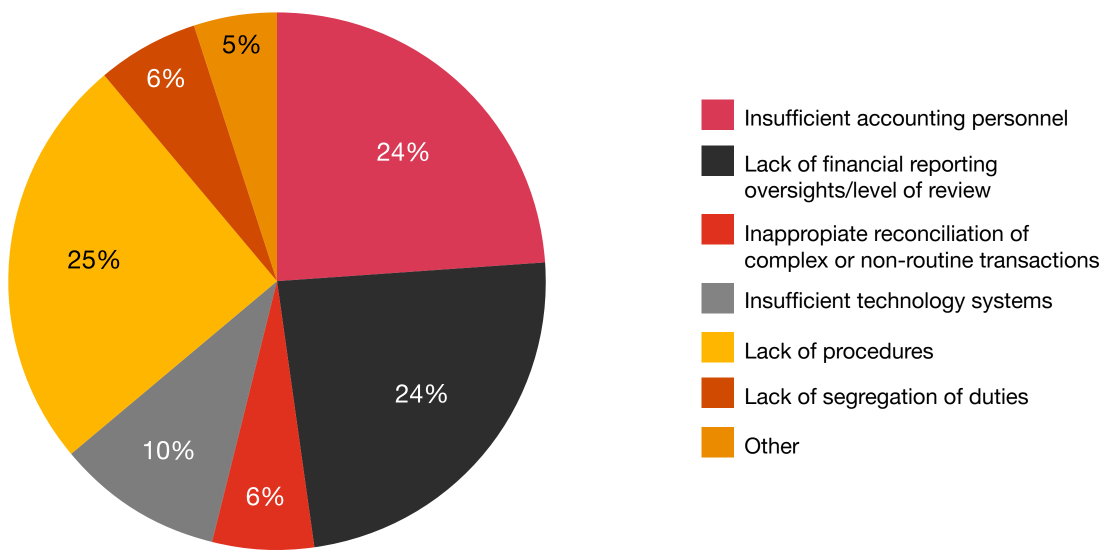


The following table shows the percentage of companies disclosing an MW within each revenue category and percentage of companies disclosing an MW within each deal size category.

IPOs with MW by LTM revenues	≤$500m	$500m–$1b	>$1b	Total
Industrial products	61%	33%	38%	47%
All IPOs	44%	43%	40%	43%

IPO with MW by deal value	≤$500m	>$500m	>$1b
Industrial products	45%	50%	47%
All IPOs	44%	41%	43%

Industrial products MWs by type

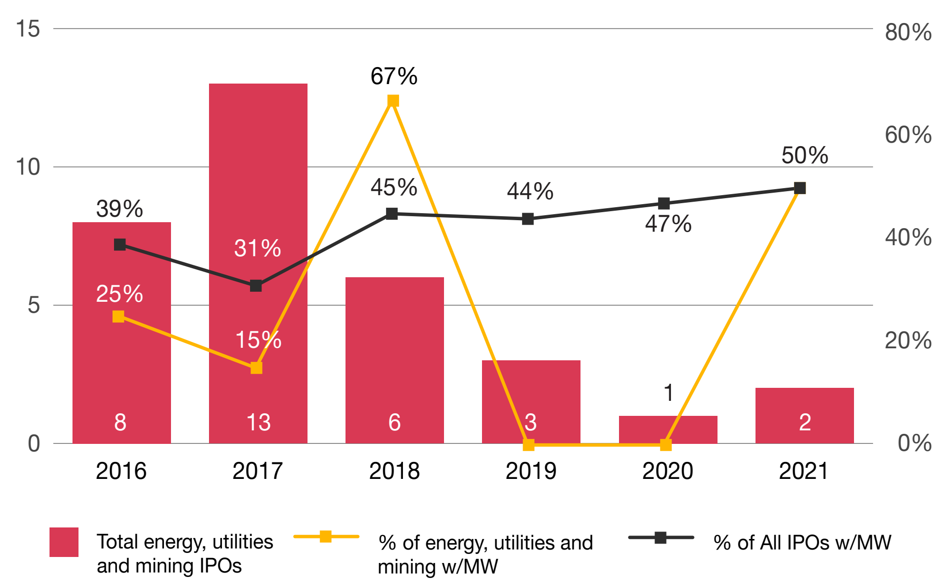


Energy, utilities and mining

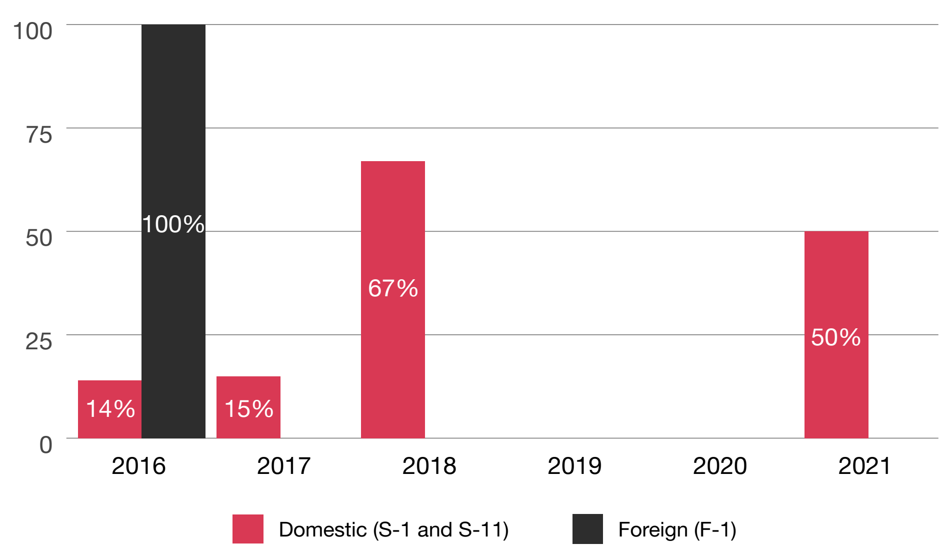
In the energy, utilities and mining sector, an average of 27% of the companies that went public disclosed at least one MW, below the 43% average of companies disclosing MWs across all sectors. Of the companies disclosing an MW, an average of 50% of foreign issuer IPOs disclosed MWs (foreign issuers represent 6% of sector IPOs) compared with an average of 22% of domestic issuers disclosing MWs. Since 2016, 33% of energy, utilities and mining IPOs with a deal value of $500 million or less reported MWs (these companies represented 62% of total energy, utilities and mining IPOs) and 28% of energy, utilities and mining IPOs with revenues of less than $500 million reported MWs (these companies represented 78% of total energy, utilities and mining IPOs).

The volume of IPOs in this sector is relatively small with only 33 IPOs out of 864 since 2016 which represent only 4% of all IPOs, with a notable decrease in sector IPOs since 2017 which is largely a factor of declining oil prices.

Energy, utilities and mining IPOs and MW disclosures



Percentage of energy, utilities and mining IPOs by issuer type disclosing MW

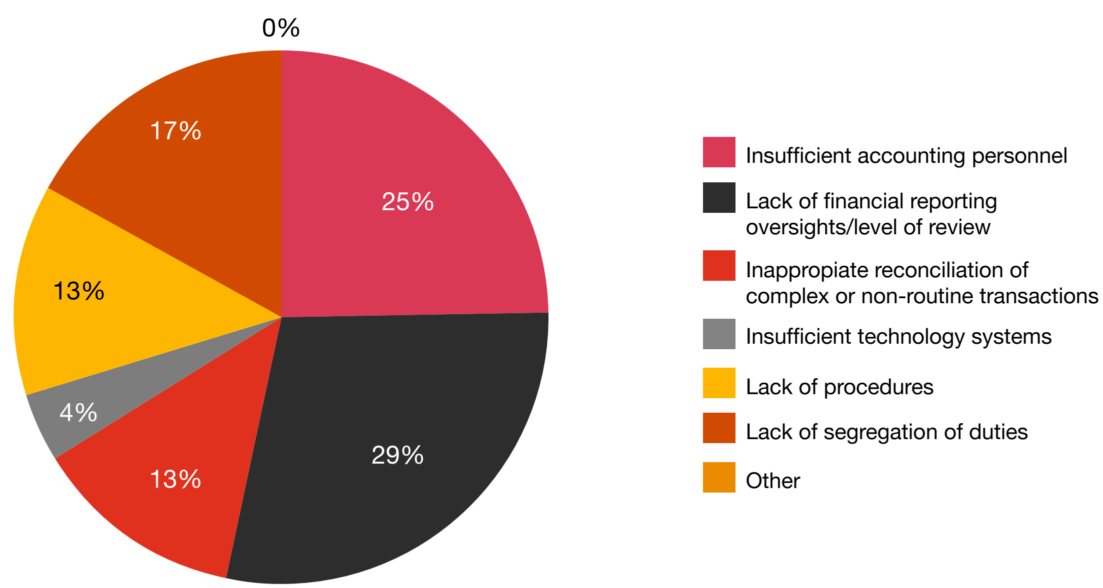


The following table shows the percentage of companies disclosing an MW within each revenue category and percentage of companies disclosing an MW within each deal size category.

IPOs with MW by LTM revenues	≤$500m	$500m–$1b	>$1b	Total
Energy, utilities and mining	28%	33%	20%	27%
All IPOs	44%	43%	40%	43%

IPO with MW by deal value	≤$500m	>$500m	>$1b
Energy, utilities and mining	33%	0%	27%
All IPOs	44%	41%	43%

Energy, utilities and mining MWs by type

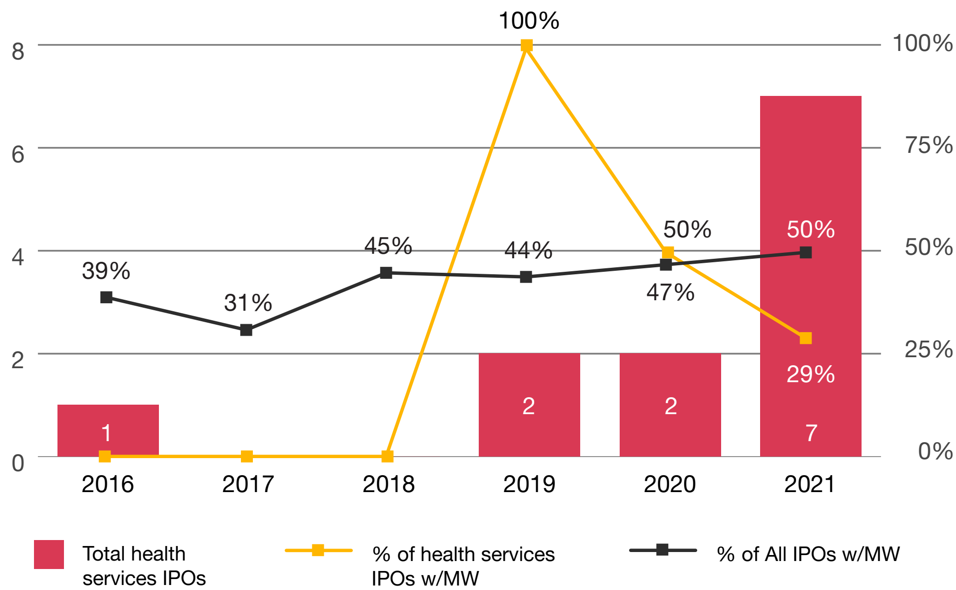


Health services

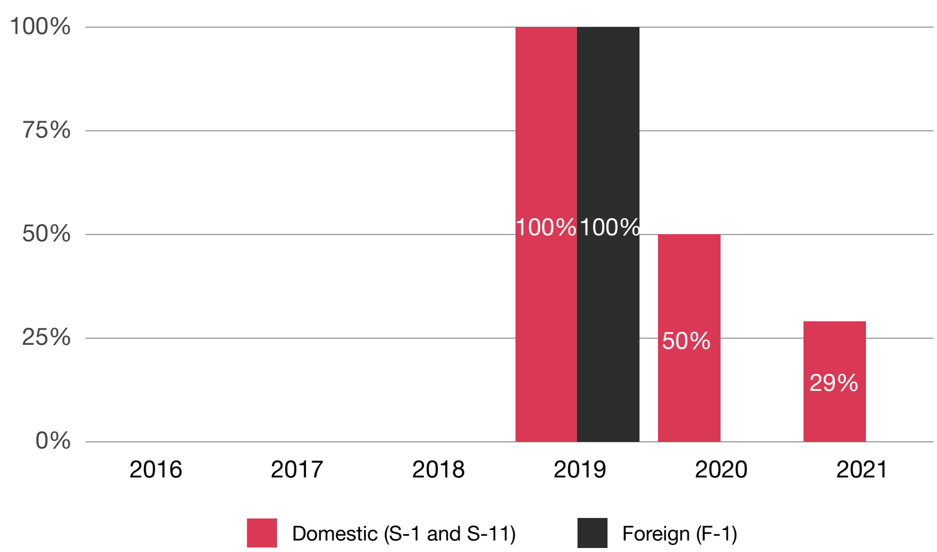
In the health services sector, an average of 42% of the companies that went public disclosed at least one MW, slightly lower than the 43% average of companies disclosing MWs across all sectors.

The volume of IPOs in this sector is small, accounting for only 12 out of 864 IPOs since 2016

Health services IPOs and MW disclosures



Percentage of health services IPOs by issuer type disclosing MW

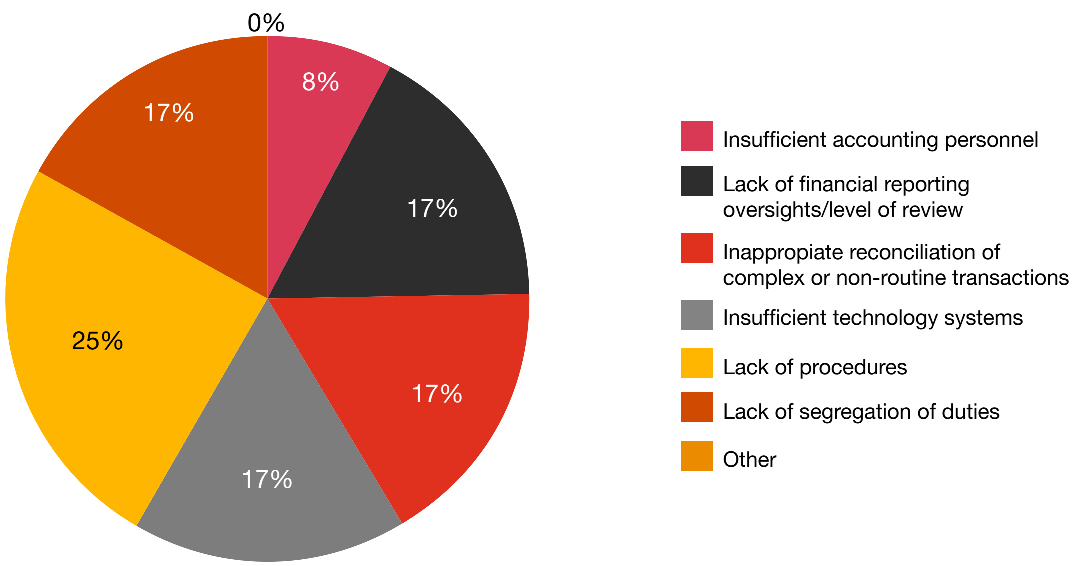


The following table shows the percentage of companies disclosing an MW within each revenue category and percentage of companies disclosing an MW within each deal size category.

IPOs w/ MW by LTM revenues	≤$500m	$500–$1,000m	>$1,000m	Total
Health services	80%	0%	n/a	42%
All IPOs	44%	43%	40%	43%

IPO with MW by deal value	≤$500m	>$500m	Total
Health services	38%	n/a	42%
All IPOs	44%	41%	43%

Health services MWs by type



What does this mean for my IPO?

Going public is a monumental decision for any company, and can forever change how a company does business. However, the IPO is not an end in itself, but the start of a new life as a public company. The most successful companies operate as if they were public companies prior to going public.

Companies are increasingly reporting MWs in their IPOs as a result of an increased demand for transparency on risks investors will face. However, disclosure of MWs, combined with disclosures regarding remediation plans and demonstrating progress toward remediation, gives investors confidence in a company's ability to function as a public company. This also gives investors a favorable impression of management as it demonstrates credibility and transparency. Additionally, it mitigates the risk of disclosing a MW subsequent to going public, which could have other consequences, including loss in credibility of management.

Given all these factors, management works with advisors on an overall readiness assessment, which will also help management determine what gaps in their internal controls and processes need to be filled before they undergo the seismic change of taking their company public. Waiting until the registration statement is being prepared and marketed to address ICFR makes for a challenging IPO process. Many companies have found that they require significant process changes to effectively implement a strong internal control framework: waiting to address Sarbanes-Oxley requirements can create a huge burden for staff whose time is better spent preparing the filing statements and coordinating with banks and underwriters.

We typically see companies start assessing and stabilizing their control environment processes 18 to 24 months prior to going public, and in our experience, companies that operate under public company rules (i.e., SOX compliance) for 6 to 12 months prior to going public have less risk of identifying internal control issues and related disclosures in their filings once they become public. Demonstrating SOX compliance prior to going public shows management's commitment to protecting stakeholder value.

Additionally, understanding end-to-end processes related to significant accounts and business processes helps management identify material risks of financial statement errors, IT dependencies and service organizations. This information is used to then design effective controls to address those risks. It is also important to note that the risk assessment should not be an exercise performed only once but a continuous exercise to monitor changes in the control environment to proactively implement or update processes and controls to fit the needs of the company and address the financial risks. A robust risk assessment, control design and testing process can help avoid material weakness in a company's control environment.

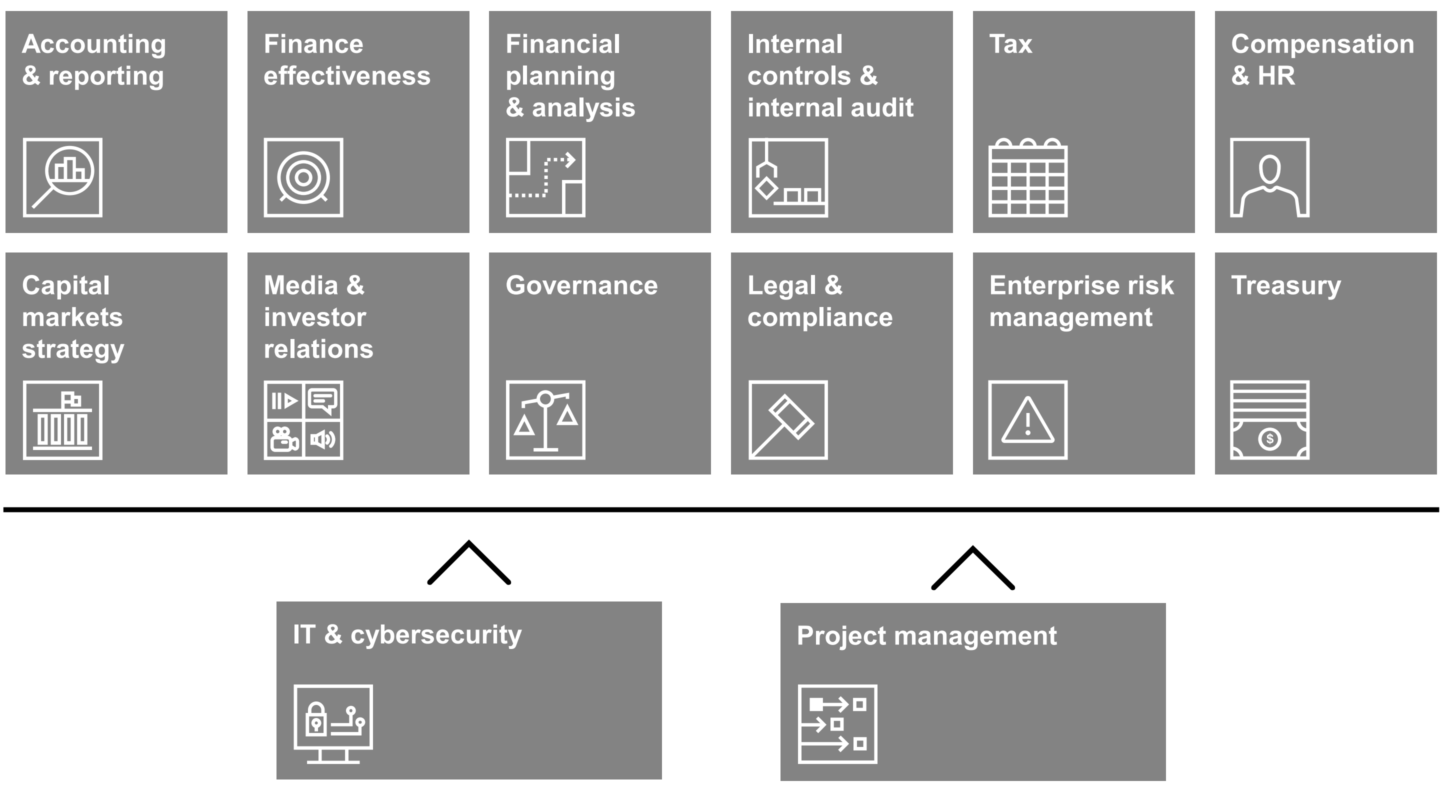
PwC's IPO services

An IPO readiness assessment is a critical step in becoming IPO ready, as it will allow management to:

- focus more time and effort where it adds the most value (i.e., the ongoing business operations);
- anticipate issues and avoid untimely delays, which can diminish the market's confidence in management, damage the company's brand, raise the overall cost of capital and, ultimately, lower the value of the IPO if market pricing windows are missed;
- assess objectively and professionally the state of readiness for life as a public company; and
- manage the two concurrent work streams of going public and being public effectively, in addition to the company's day-to-day operations.

PwC brings an integrated solution to evaluate your organization across the major functions to identify functional areas that may need to be created or enhanced prior to being public-company-ready. We can advise management in critical areas as they implement those changes and the company undergoes the transformation from private entity to public equity filer.

The chart below illustrates many of the areas an organization will need to focus on and improve as it embarks on the going-public process and transitions to operating as a public company.



Contacts

For a deeper discussion, please contact one of our practice leaders or your local Deals partner/managing director:

Mike Bellin
(720) 361 9294
michael.j.bellin@pwc.com
US IPO Services Co-Lead

David Ethridge
(212) 845 0739
david.a.ethridge@pwc.com
US IPO Services Co-Lead

Alan Jones
(646) 471 3700
alan.jones@pwc.com
Bay Area Northwest Market Managing Partner

Erin Cahill
(954) 205 2047
erin.e.cahill@pwc.com
Partner, Deals

Shane Foley
(201) 245 8090
shane.p.foley@pwc.com
Partner, Risk & Compliance

Daniel Klausner
(646) 471 5388
daniel.h.klausner@pwc.com
Managing Director, Deals

Monica Nayar
(510) 209 5248
monica.nayar@pwc.com
Partner, Risk & Compliance

Authors:
Simona Codreanu
(617) 840 3845
simona.r.codreanu@pwc.com
Director, Deals

Patrick Kella
(636) 236 3106
patrick.j.kella@pwc.com
Manager, Deals

www.pwc.com