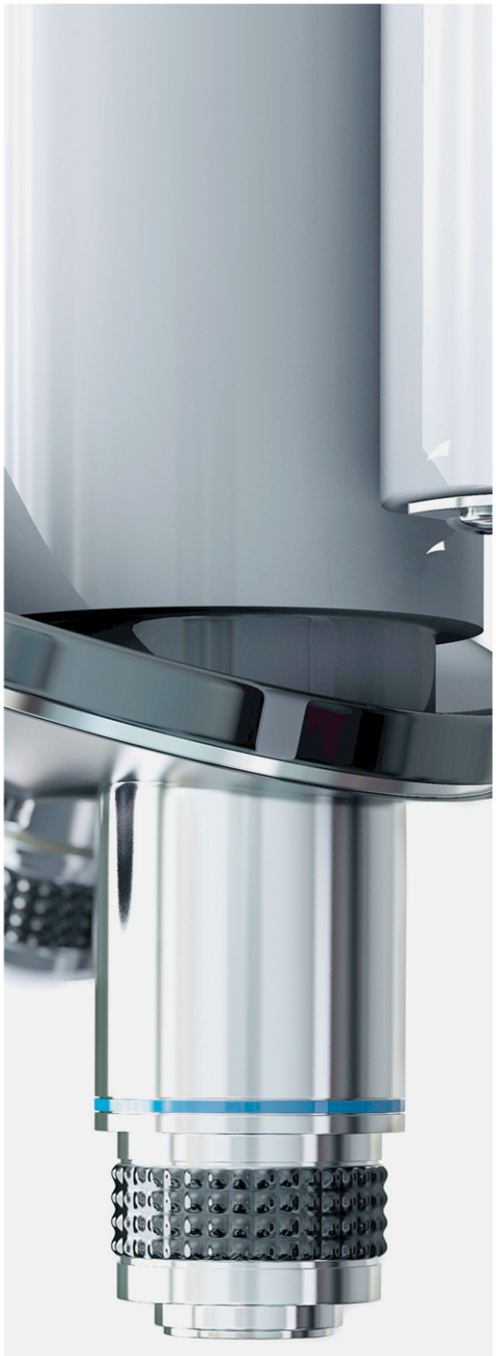

PAUL HASTINGS

IPOs in the JOBS Act Era 2014

Global Securities and Capital Markets Group

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ABOUT PAUL HASTINGS

Paul Hastings provides innovative legal solutions to many of the world's leading companies and financial institutions in markets across Asia, Europe, Latin America, and the United States. We offer a complete portfolio of services to support our clients' complex, often mission-critical needs—from structuring first-of-their-kind transactions to resolving complicated disputes to providing the savvy legal counsel that keeps business moving forward. We are proud to consistently rank among the best firms in top legal publications such as *The American Lawyer, Chambers and Partners*, and *Legal 500*, and recently placed first on The *American Lawyer's* 2014 A-List of the 20 Most Successful Law Firms in America.

ABOUT THE SURVEY

Welcome to the inaugural edition of **IPOs in the JOBS Act Era 2014**, published by Paul Hastings. The implementation of the JOBS Act has significantly simplified the initial public offering (IPO) process for many companies. In the two years since the JOBS Act was signed into law, the annual number of U.S. IPOs has reached its highest level since 2007. Although market factors played a role, it is clear that the accommodations offered to IPO issuers under the JOBS Act have been critical factors in many companies' decision to "go public." Many of the JOBS Act provisions are already firmly embedded in the U.S. IPO landscape.

In our in-depth study, we examine the corporate governance practices and disclosures of 100 U.S.-based Emerging Growth Companies that completed an IPO during the period from September 2012 (five months after the adoption of the JOBS Act) to August 2014. Of the surveyed issuers, 48 are in the technology sector and the remaining 52 are in the life sciences sector.

Key findings of our report include:

- Nearly all surveyed issuers elected to submit at least one Registration Statement on Form S-1 on a confidential basis.
- The median number of days between the first public filing of the Form S-1 and the IPO effective date among surveyed issuers was 39 days, as opposed to a median of 101 days between the date of the first confidential submission of the draft Form S-1 and the IPO effective date.
- Nearly all surveyed issuers used one or more of the reduced executive compensation disclosure accommodations, including omitting a Compensation Discussion and Analysis (CD&A) section.
- Most of the surveyed issuers irrevocably elected not to take advantage of phase in rules for new or revised financial accounting standards.
- Only a small majority of the surveyed issuers elected to take advantage of the opportunity to provide two years of audited financials, rather than three years.
- Approximately half of the surveyed issuers elected to provide only two years of selected historical financial statements.
- Despite pressure to modify these practices at public issuers, most of the surveyed issuers adopted a classified board of directors, plurality voting in director elections and supermajority voting requirements to amend or eliminate defense measures in the issuers' governing documents.
- 20% of the surveyed IPOs included a resale (selling stockholder) component.

- On average, approximately 75% of the surveyed issuers' boards of directors qualified as independent under applicable stock exchange requirements at the time of the IPO.
- More than half of the surveyed issuers adopted a forum selection clause for the resolution of specified disputes.
- Over 90% of the new equity incentive plans adopted by surveyed issuers in connection with the IPO included an evergreen (share replenishment) feature.

We hope you will find our study informative and helpful. If you would like to discuss our findings or learn more about how Paul Hastings partners with clients to achieve outstanding outcomes, please contact any of our Capital Markets lawyers.

JOBS Act Background

Historically, the IPO process was the same for all companies, regardless of size, which many believe contributed to a decrease in the number of IPOs by smaller companies. To address this, the JOBS Act created a new class of public companies called "Emerging Growth Companies" (EGCs). An issuer qualifies as an EGC if it had less than $1 billion in annual gross revenues during its most recently completed fiscal year, subject to certain exceptions, and conducts its IPO after December 8, 2011.

Under the JOBS Act, for as long as an issuer remains an EGC, the issuer will be entitled to a number of exemptions from corporate governance and reporting requirements that continue to be applicable to non-EGCs. These include the following:

- EGCs may confidentially submit a draft registration statement to the Securities and Exchange Commission (SEC), for confidential nonpublic review, prior to filing the registration statement publicly, provided that the initial confidential draft registration statement submitted to the SEC and all amendments thereto are publicly filed at least 21 days prior to conducting the road show for the IPO.

- EGCs may communicate with qualified institutional buyers and accredited investors to gauge investor appetite before the filing of a registration statement with the SEC, often referred to as "testing the waters." This allows EGCs to discuss a contemplated offering without being subject to many of the quiet period "gun-jumping" restrictions on pre-offering communications imposed by the SEC.

- EGCs may provide less disclosure in their IPO registration statements and prospectuses, including:

  - only two years of audited historical financial statements (instead of three);

  - selected financial data only from the earliest audit period presented in the IPO registration statement and therefore for a period as short as two years (instead of the previous five years); and

  - only the limited executive compensation disclosure applicable to smaller reporting companies (whether or not the issuer qualifies as a "smaller reporting company," as defined in Rule 12b-2 under the Securities Exchange Act of 1934, as amended (Exchange Act).

- EGCs are also exempt from the following requirements:

  - the auditor attestation requirements in Section 404(b) of the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley Act) regarding internal control over financial reporting;

  - holding say-on-pay votes and disclosing certain executive compensation information (such as pay versus performance ratios);

  - complying with any new or revised accounting standards under U.S. generally accepted accounting principles (GAAP), until such standards become applicable to private companies; and

- complying with any new Public Company Accounting Oversight Board (PCAOB) rules requiring mandatory audit firm rotation or a supplement to the auditor's report.

Under the JOBS Act, an EGC will lose its EGC status upon the *earliest* of:

- the last day of the first fiscal year in which the issuer's annual gross revenues exceed $1 billion;
- the last day of the fiscal year in which the fifth anniversary of the issuer's first sale of equity securities pursuant to an effective registration statement occurs;
- the date on which the issuer has, during the previous three-year period, issued more than $1 billion in non-convertible debt; and
- the date on which the issuer is deemed to be a "large accelerated filer," as defined in Rule 12b-2 under the Exchange Act (principally issuers with at least $700 million of non-affiliate common equity market capitalization as of the last business day of their most recently completed second fiscal quarter).

JOBS Act Disclosure

An EGC must identify itself as an EGC on the cover page of the IPO prospectus. Through the comment letter process, the Staff of the SEC also requires an issuer to disclose whether it is electing to take advantage of the extended transition period for complying with new or revised accounting standards. Most issuers include disclosure regarding EGC status and one or more JOBS Act provisions in the following sections of the IPO prospectus: on the cover page; in the "box" summary; in the risk factors and Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) sections; and, in some cases, as part of the discussion regarding executive compensation.

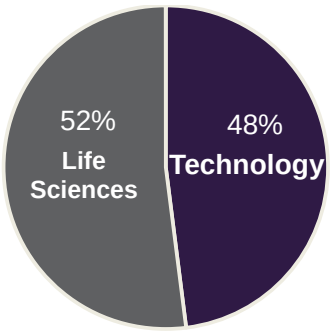
Methodology

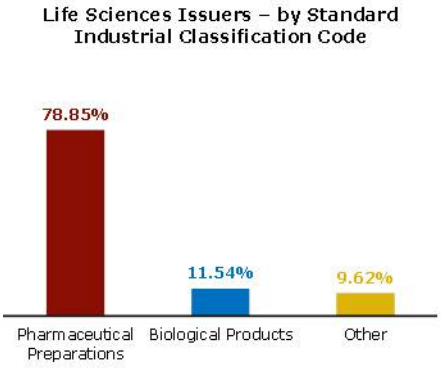
We examined the corporate governance practices and disclosures of 100 U.S.-based EGCs that completed an IPO during the period from September 2012 (five months after the adoption of the JOBS Act) to August 2014. Of the surveyed issuers, 48 are in the technology sector and the remaining 52 are in the life sciences sector. We determined whether an issuer is in the technology or life sciences sector based on the issuer's standard industrial classification code. None of the surveyed issuers qualified or elected to be treated as a "controlled company," as defined under New York Stock Exchange and Nasdaq Stock Market LLC listing standards, or qualified as a "foreign private issuer," as defined under Rule 405 of the Securities Act of 1933, as amended, and Rule 3b-4 under the Exchange Act. Among the surveyed issuers, 98 were incorporated in the State of Delaware. Data was compiled based on publicly-available information obtained through the SEC's Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system.

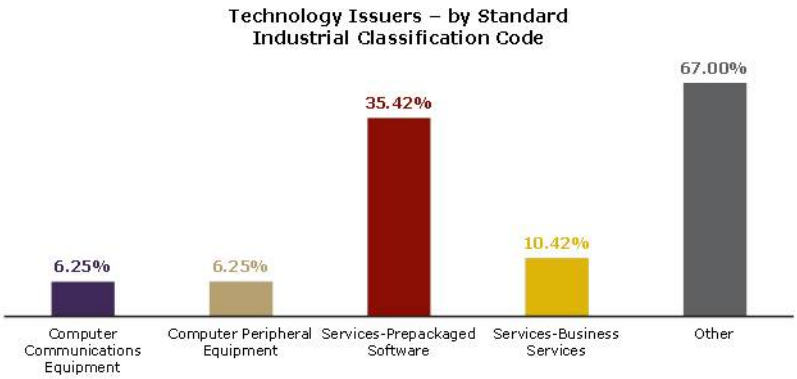
The Issuers

We examined the IPOs of the following 100 issuers.

Sector: Technology vs. Life Sciences







A10 Networks, Inc.
Acceleron Pharma Inc.
Aerie Pharmaceuticals, Inc.
Agile Therapeutics, Inc.
Agios Pharmaceuticals, Inc.
Alder BioPharmaceuticals, Inc.
Ambit Biosciences Corporation
Amphastar Pharmaceuticals, Inc.
Applied Optoelectronics, Inc.
Aratana Therapeutics, Inc.
Ardelyx, Inc.
Arista Networks, Inc.
Avalanche Biotechnologies, Inc.
Barracuda Networks, Inc.
BIND Therapeutics, Inc.
bluebird bio, Inc.
Castlight Health, Inc.
Chegg, Inc.
Chimerix, Inc.
Conatus Pharmaceuticals Inc.
Control4 Corporation
Coupons.com Incorporated
Covisint Corporation
Cvent, Inc.
Cyan, Inc.
Enanta Pharmaceuticals, Inc.
Epizyme, Inc.
Esperion Therapeutics, Inc.
Evoke Pharma, Inc.
Fate Therapeutics, Inc.
FireEye, Inc.
Five Prime Therapeutics, Inc.
Five9, Inc.
Gigamon Inc.
GoPro, Inc.
Intercept Pharmaceuticals, Inc.
Intersect ENT, Inc.
Intrexon Corporation
Karyopharm Therapeutics Inc.
Kindred Biosciences, Inc.
Kite Pharma, Inc.
KYTHERA Biopharmaceuticals, Inc.
LifeLock, Inc.
NanoString Technologies, Inc.
Nimble Storage, Inc.
Omthera Pharmaceuticals, Inc.
OncoMed Pharmaceuticals, Inc.
Onconova Therapeutics, Inc
GrubHub Inc.
HealthEquity, Inc.
Heat Biologics, Inc.
Immune Design Corp.
Imprivata, Inc.
Loxo Oncology, Inc.
MacroGenics, Inc.
Marin Software Incorporated
Marketo, Inc.
Mavenir Systems, Inc.
Minerva Neurosciences, Inc.
MobileIron, Inc.
Model N, Inc.
Ophthotech Corporation
Pfenex Inc.
Portola Pharmaceuticals, Inc.
PTC Therapeutics, Inc.
Qualys, Inc.
Rally Software Development Corp.
Receptos, Inc.
Regado Biosciences, Inc.
Regulus Therapeutics Inc.
Relypsa Inc.
RetailMeNot, Inc.
RingCentral, Inc.
Rocket Fuel Inc.
Ruckus Wireless, Inc.
Sage Therapeutics, Inc.
SCYNEXIS, Inc.
Shutterstock, Inc.
Signal Genetics, Inc.
SolarCity Corporation
Tableau Software, Inc.
Tandem Diabetes Care, Inc.
TetraLogic Pharmaceuticals Corporation
Tetraphase Pharmaceuticals, Inc.
Textura Corporation
The ExOne Company
TrueCar, Inc.
Trulia, Inc.
TubeMogul, Inc.
Twitter, Inc.
Veracyte, Inc.
Violin Memory, Inc.
Workday, Inc.
Xencor, Inc.
xG Technology, Inc.
Xoom Corporation
YuMe, Inc.
Zafgen, Inc.
Zendesk, Inc.
zulily, inc.

The Role of Proxy Advisory Firms

Institutional investors frequently retain the services of proxy advisory firms to assist the investors with assessing companies' annual stockholder meeting proposals, corporate governance practices and related matters. In some cases, proxy advisory firms are given authority to execute proxies or voting instructions on behalf of their institutional investor clients. Some proxy advisory firms qualitatively rate or score issuers based on judgments about the issuer's governance structure, policies and practices. Institutional Shareholder Services (ISS) and Glass Lewis & Co. (Glass Lewis) hold the largest share of the proxy advisory services market. Anecdotal data suggests that these firms can influence more than 40% of the stockholder vote at some public companies.

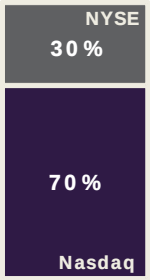
Although proxy advisors are not engaged to review an issuer prior to its IPO, IPO issuers should be cognizant of the proxy advisors' positions on key corporate governance measures. In the event an IPO issuer's disclosed practices and procedures diverge from some of the proxy advisors' recommendations for public companies, institutional investors may ask the issuer to justify these practices and procedures during the IPO road show. Moreover, newly public companies may see some of their corporate governance provisions adopted in connection with the IPO under attack by proxy advisors – namely, ISS and Glass Lewis – as early as at the first annual meeting of stockholders following the IPO.

We have noted in this survey the current positions of ISS and Glass Lewis with respect to some of the corporate governance provisions typically adopted by IPO issuers.

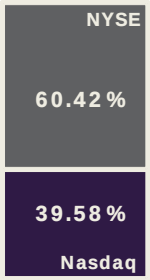
IPOS IN THE JOBS ACT ERA

STOCK EXCHANGE

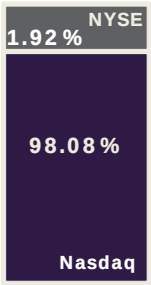
Stock Exchange: NYSE vs. Nasdaq



Stock Exchange – Technology Issuers: NYSE vs. Nasdaq



Stock Exchange – Life Sciences Issuers: NYSE vs. Nasdaq

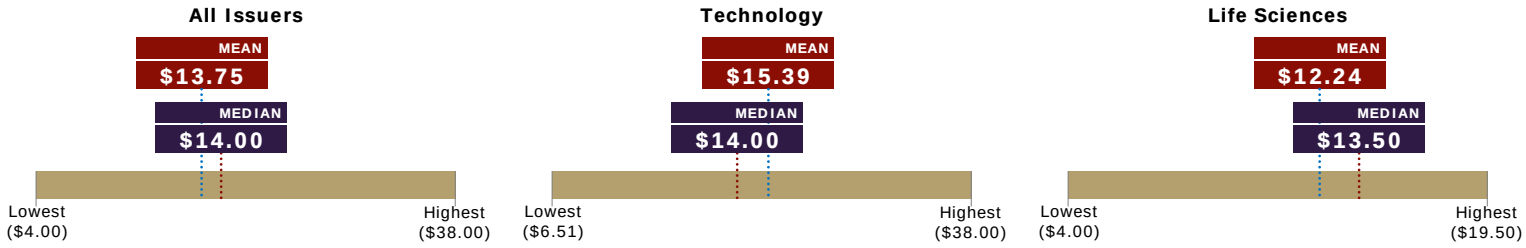


The NYSE Market (NYSE) has multiple listing markets. Most IPO issuers listing with the NYSE trade on the New York Stock Exchange, often referred to as the "Big Board." The NYSE MKT LLC is an NYSE market tailored to smaller and mid-sized companies and was created through the NYSE's acquisition of the American Stock Exchange in 2008. The listing and maintenance requirements for the NYSE MKT LLC are less burdensome than the requirements of the New York Stock Exchange.

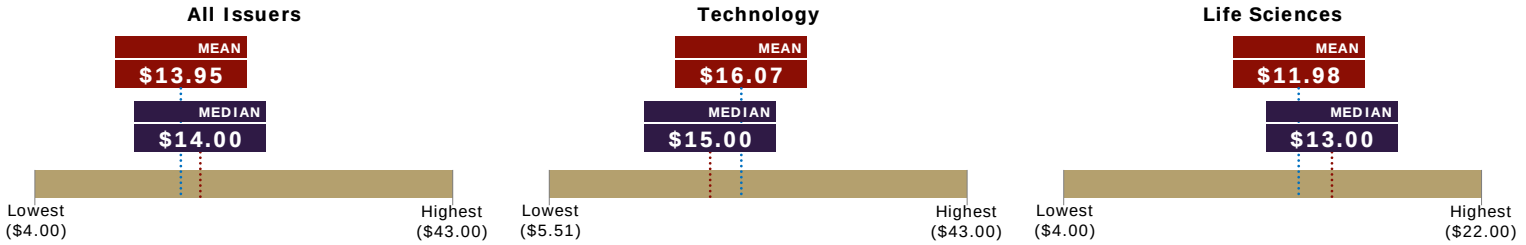
The Nasdaq Stock Market LLC (Nasdaq) is comprised of three distinct listing markets: The Nasdaq Capital Market (formerly called the Nasdaq SmallCap Market); The Nasdaq Global Market (formerly called the Nasdaq National Market); and The Nasdaq Global Select Market. Each of the markets has its own listing requirements and fee structure. The Nasdaq Global Select Market has more demanding listing standards than the other Nasdaq markets and is generally reserved for issuers that have been publicly traded for some period of time, rather than issuers listing in connection with an IPO. The Nasdaq Global Market contains more rigorous listing standards than The Nasdaq Capital Market and is the market on which most IPO issuers commence their Nasdaq listing. The Nasdaq Capital Market is tailored to smaller and mid-sized IPO issuers.

IPO TERMS

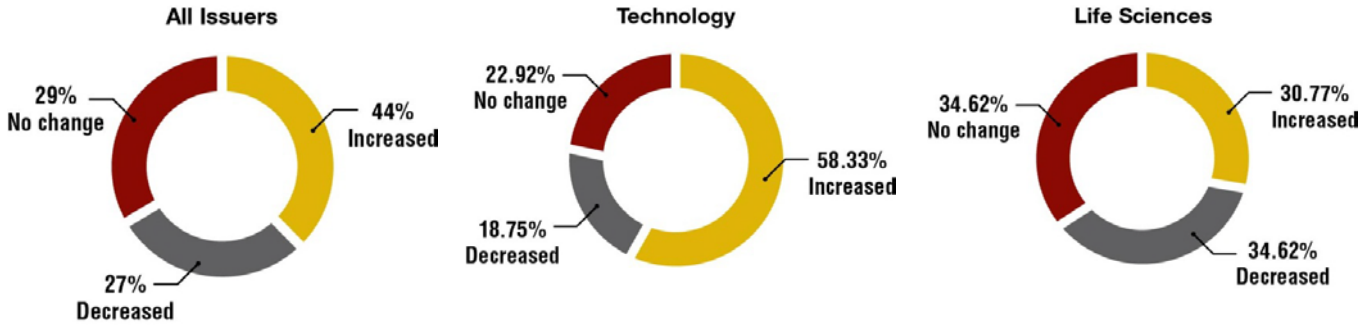
Estimated IPO Price Per Share



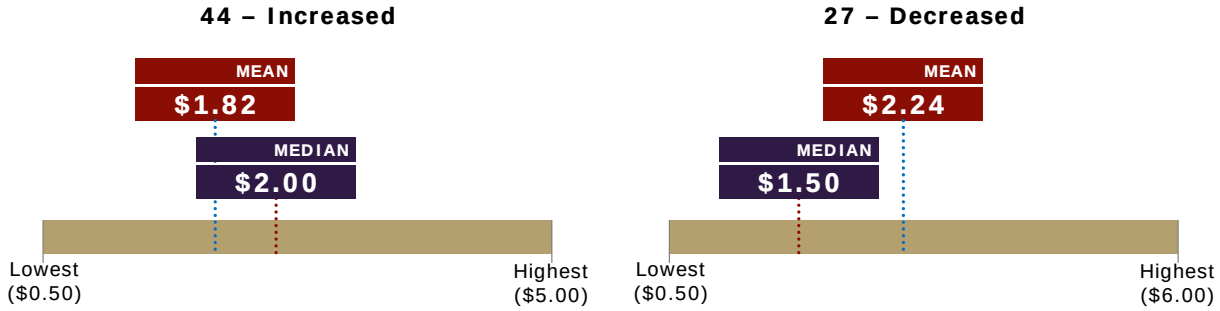
Final IPO Price Per Share



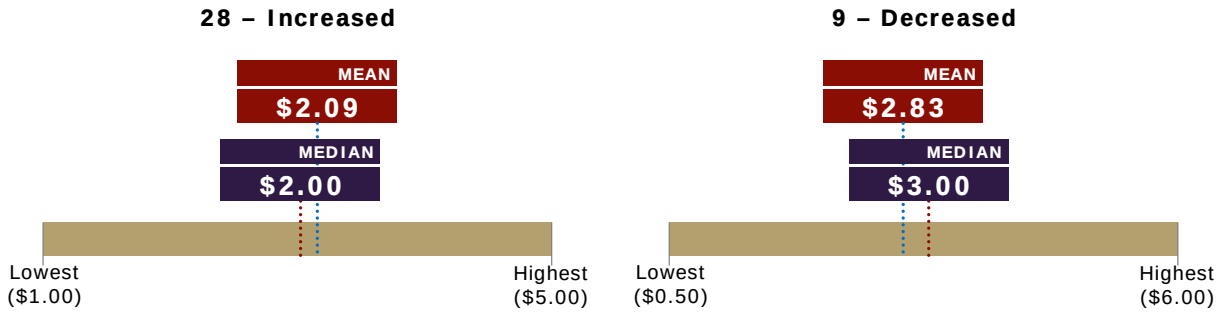
Price Changes from Midpoint



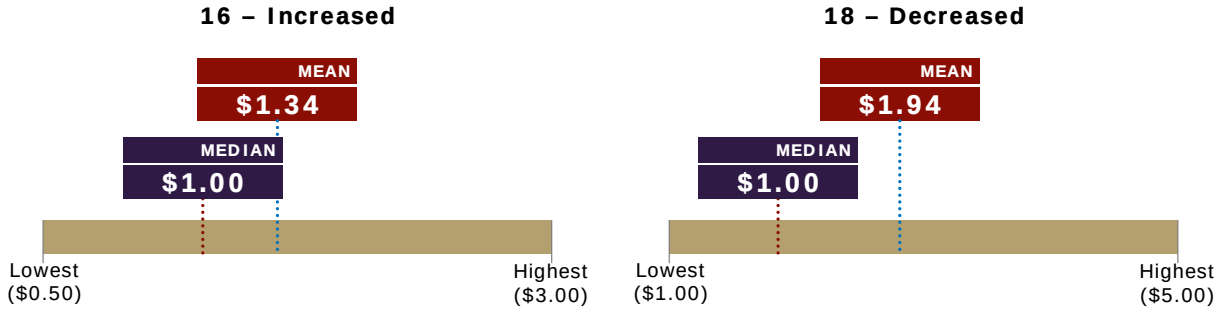
Range of Price Changes
All Issuers



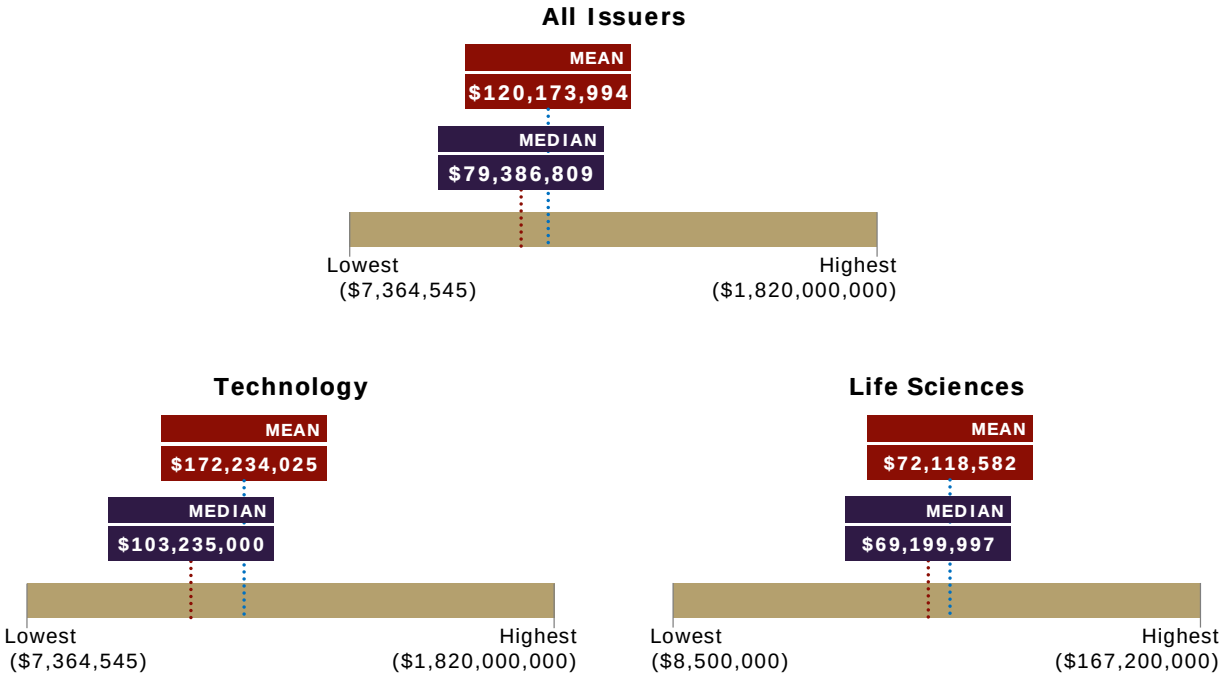
Range of Price Changes
Technology



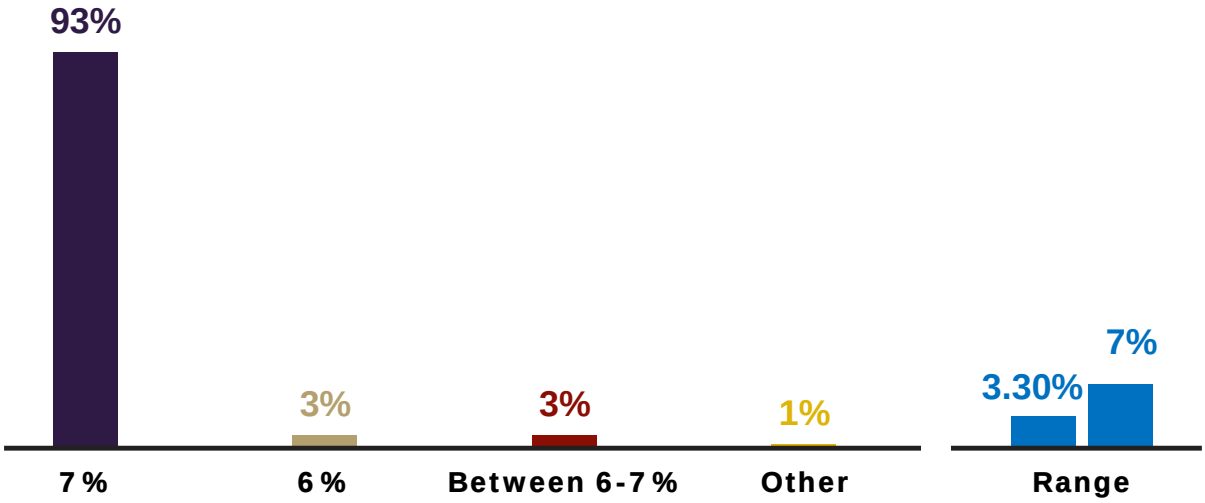
Range of Price Changes
Life Sciences



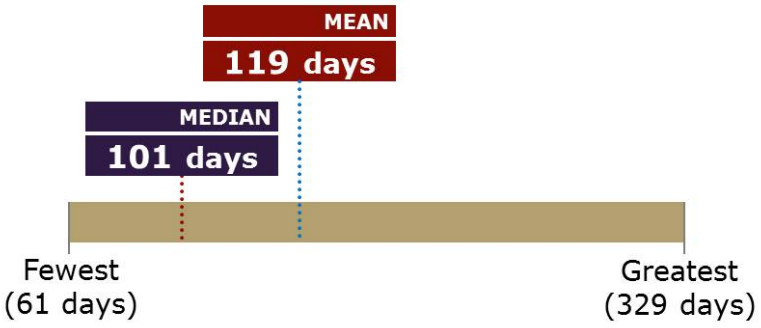
IPO Gross Proceeds



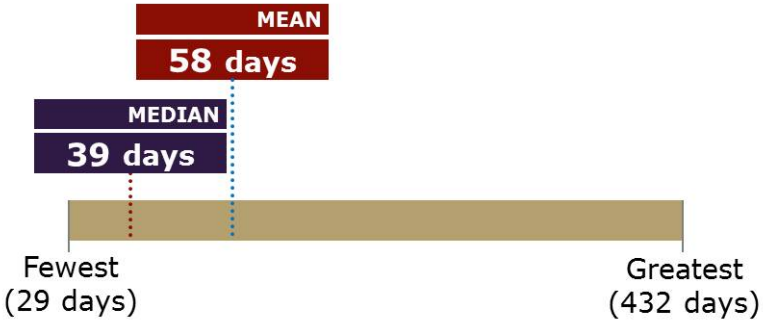
Underwriting Discount



Days in Registration
(from 1st confidential submission)



Days in Registration
(from 1st public filing)

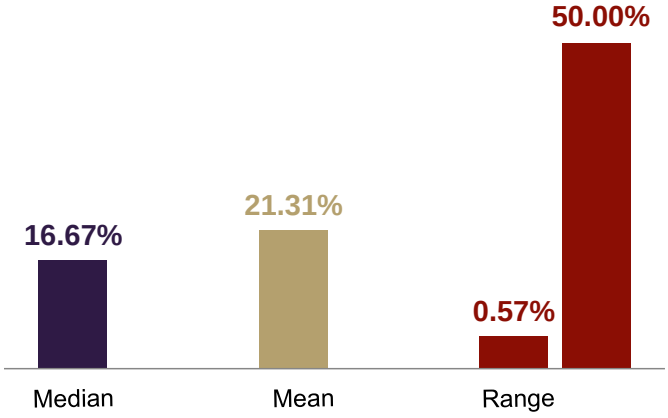


Primary and Secondary Shares

A primary offering consists of the sale of newly issued shares by the issuer. A secondary offering consists of the sale of already issued shares owned by the issuer's stockholders. IPOs can be structured as exclusively primary offerings, exclusively secondary offerings or a combination of primary and secondary offerings. Occasionally, secondary shares are reserved for sale only pursuant to the over-allotment option provided to the underwriters in the IPO (often referred to as the "green shoe" or "shoe"). Underwriters generally receive the same discounts and commissions for shares sold directly by the issuer and those sold by the issuer's stockholders in the IPO.

IPOs with Selling Stockholders (Secondary Offering Component)

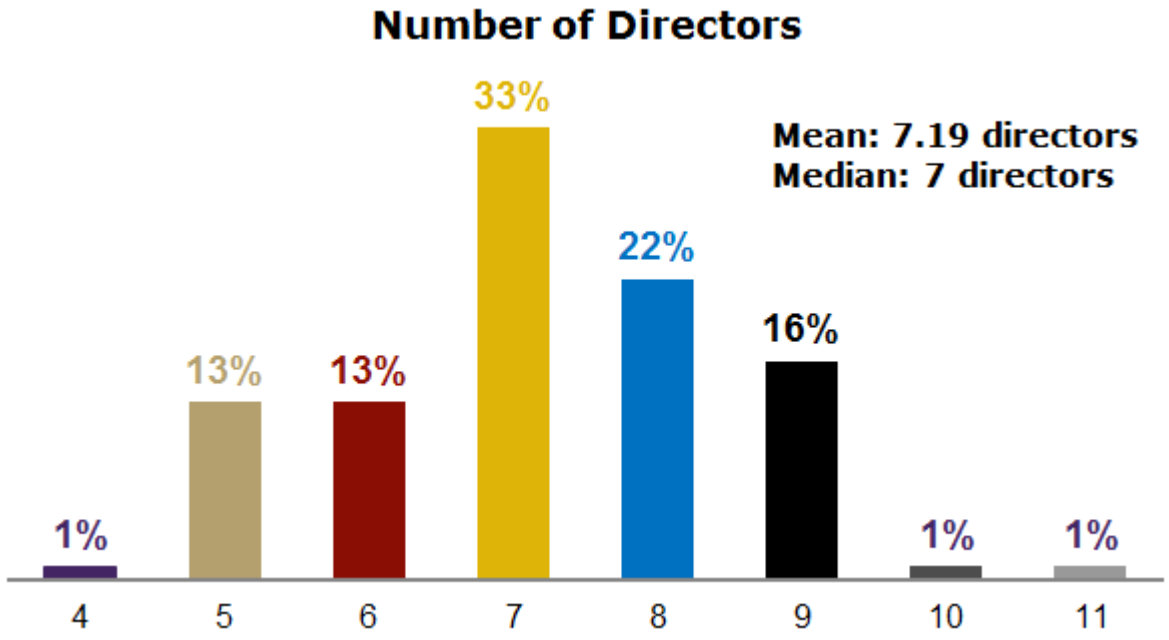
Secondary Offering Component as a Percentage of Total Offering



BOARD AND BOARD COMMITTEE MATTERS

Size of the Board of Directors

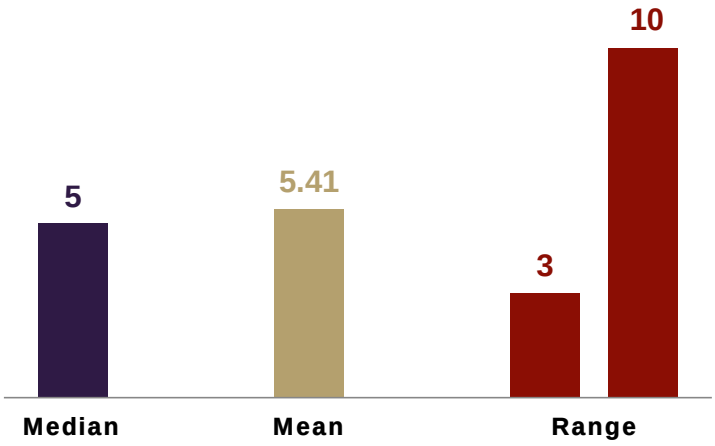
Board size represents the total number of members of the issuer's board of directors upon completion of the IPO. A main consideration in setting the authorized number of directors is ensuring the issuer has a sufficient number of independent directors (discussed below) to satisfy applicable SEC and stock exchange listing requirements. A number of surveyed issuers appointed new members to the board of directors within a short period immediately prior to or following the initial submission or filing of the IPO Registration Statement on Form S-1 with the SEC.



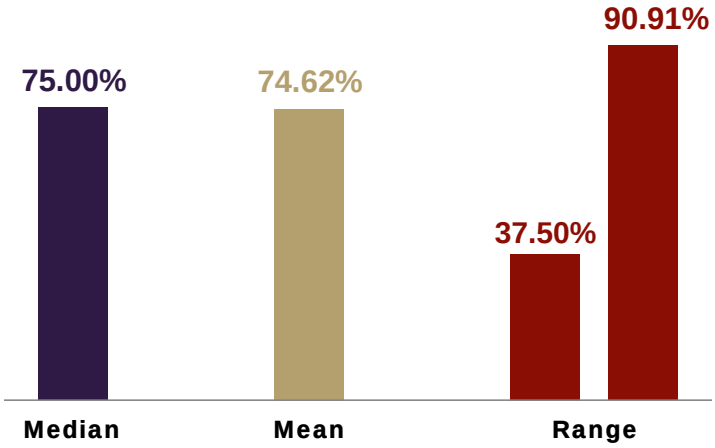
Percentage of Independent Directors

Under the rules of the NYSE and Nasdaq, unless an issuer is a "controlled company," a majority of the members of the board of directors of each NYSE and Nasdaq-listed issuer must be "independent" within one year of its initial listing date. Under NYSE rules, directors are generally considered "independent" if they have no material relationship with the listed issuer (directly or as a partner, stockholder or officer of an organization that has a relationship with the issuer). Under Nasdaq rules, directors are generally considered "independent" if they are not an executive officer or employee of the issuer or its subsidiaries or any other individual having a relationship that, in the opinion of the issuer's board of directors, would interfere with the exercise of independent judgment in carrying out the responsibilities of a director. The proxy advisors firms ISS and Glass Lewis have adopted their own definitions of director independence.

Number of Independent Directors at IPO

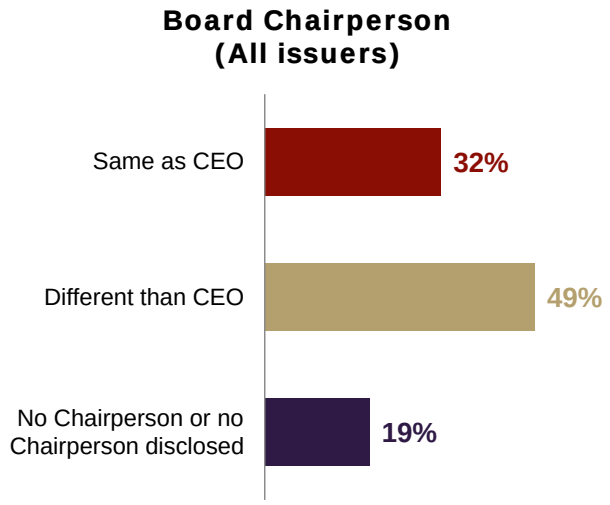


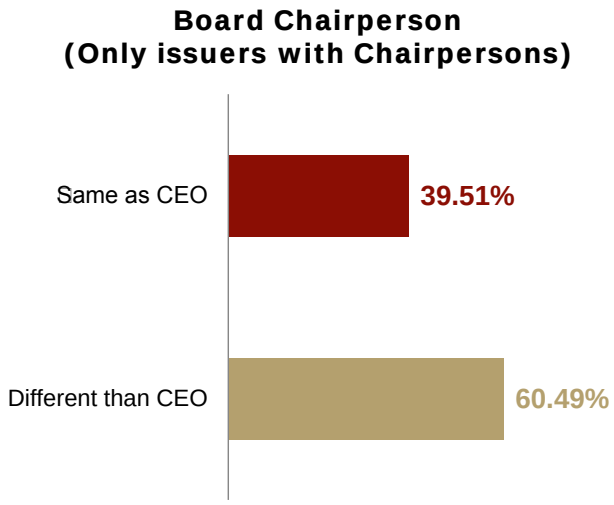
Percentage of Independent Directors at IPO



Separation of Chairman and CEO

One of the most active corporate governance questions in the public company landscape is whether to separate the roles of an issuer's chief executive officer and chairperson of the board of directors. Traditionally among U.S. corporations, the same individual held both positions. Following the passage of the Sarbanes-Oxley Act, the number of issuers that elected to separate the roles of the CEO and chairperson of the board of directors increased. Those issuers at which the same individual holds both positions frequently designate an independent director to serve as the "lead" or "presiding" director. The NYSE requires that its listed issuers have non-management directors meet at regularly scheduled executive sessions without management, overseen by a "presiding" director. In addition to supervising portions of meetings at which only the independent directors are present, lead directors often play a greater role in formulating agendas for the meetings of the board of directors and acting as a primary liaison between the board of directors and management. From 2013 through 2014 to date, stockholders have voted on approximately 120 proposals to separate the roles of CEO and chairperson of the board of directors. Approximately 10% of these proposals were approved by stockholders.





Committees of the Board of Directors

NYSE

An NYSE-listed issuer must have an independent audit committee, compensation committee and a nominating and corporate governance committee.

The audit committee must have at least one member by the issuer's listing date, at least two members within 90 days of the listing date, and at least three members within one year of the listing date. In addition, the audit committee must have at least one independent member by the listing date, at least a majority of independent members within 90 days of the effective date of the IPO registration statement, and must be fully independent within one year of the effective date of the IPO registration statement. Audit committee members are also required to meet additional independence tests set forth by the SEC.

The compensation committee must have at least one independent member by the earlier of the date the IPO closes or five business days from the issuer's listing date, at least a majority of independent members within 90 days of the listing date, and must be fully independent within one year of the listing date. Although NYSE rules do not require that the compensation committee have more than one member, most compensation committees have at least two members to meet requirements under Section 162(m) of the Internal Revenue Code of 1986, as amended, and Rule 16b-3 under the Exchange Act.

The nominating and corporate governance committee must have at least one independent member by the earlier of the date the IPO closes or five business days from the issuer's listing date, at least a majority of independent members within 90 days of the listing date, and must be fully independent within one year of the listing date. However, NYSE rules do not require that the nominating and corporate governance committee have more than one member.

All of the NYSE-listed issuers included in the survey had a standing audit committee, compensation committee and nominating and corporate governance committee in place at the time of the IPO.

Audit Committee

Compensation Committee

Nominating and Corporate Governance Committee

Nasdaq

A Nasdaq-listed issuer must have an independent audit committee and compensation committee. In addition, Nasdaq requires that director nominees be selected or recommended for selection to the issuer's board of directors by an independent nominating committee or by a majority of the independent directors. Most Nasdaq-listed issuers elect to have a separate nominating (and corporate governance) committee.

The audit committee is required to have a minimum of three members at all times. The audit committee must have at least one independent member by the issuer's listing date, at least a majority of independent members within 90 days of listing, and must be fully independent within one year of listing. Audit committee members are also required to meet additional independence tests set forth by the SEC.

The compensation committee is required to have a minimum of two members at all times. The compensation committee must have at least one independent member by the issuer's listing date, at least a majority of independent members within 90 days of listing, and must be fully independent within one year of listing.

If an issuer elects to establish a nominating committee, the committee must have at least one independent member by the issuer's listing date, at least a majority of independent members within 90 days of listing, and must be fully independent within one year of listing.

All of the Nasdaq-listed issuers included in the survey had a standing audit committee, compensation committee and nominating and corporate governance committee in place at the time of the IPO.

Other Committees

As they mature, many public companies will create additional standing committees of the board of directors to address changing needs and demands. These may include a separate compliance committee, risk management committee, executive committee, strategy committee and technology committee, among others. Only one of the surveyed issuers disclosed that it had an additional committee of the board of directors in place at the time of its IPO.

Other Board Committee

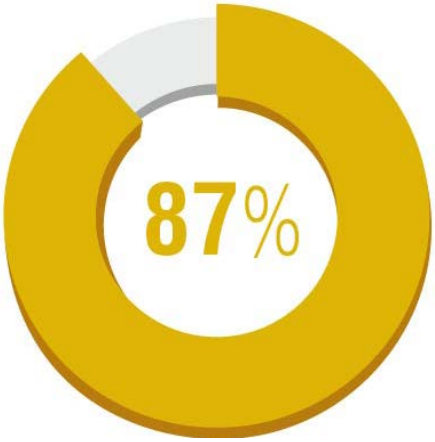
DEFENSE MEASURES

Classified / Staggered Board of Directors

Most of the surveyed issuers implemented a classified board of directors, commonly referred to as a staggered board of directors, in connection with their IPO. Under a classified board of directors, the board is typically divided into three classes where approximately one-third of the members of the board of directors is elected each year and each director serves a three-year term. Classified boards preserve company stability and continuity of management and act as a defense mechanism by eliminating a potential acquiror's ability to replace an entire board of directors at one annual meeting of the issuer's stockholders. An acquiror would need to replace board members at at least two consecutive annual meetings of stockholders in order to take control of a board of directors.

Proxy advisory firms and a number of institutional stockholders oppose classified boards of directors. These groups believe that classified boards entrench directors and that nominating all directors for election of stockholders on an annual basis increases director accountability and, therefore, issuer performance. Stockholder proposals to declassify boards of directors at public companies continue to be one of the most common annual stockholder meeting proposals each year. In both 2013 and 2014 to date, more than 90% of the proposals to declassify boards of directors were approved by stockholders.

Classified / Staggered Board

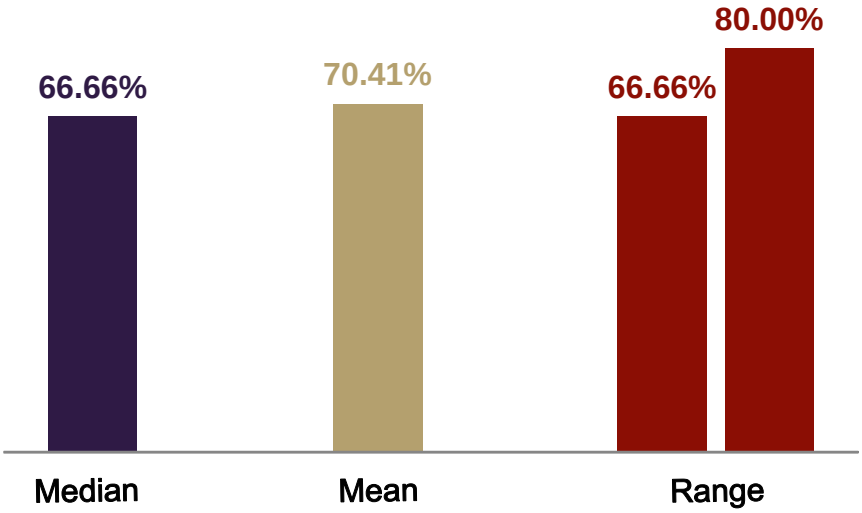


Limitation on Right to Remove Directors

Under the corporate laws of most states, including Delaware, directors can be removed, with or without cause, by the holders of a majority of the shares entitled to vote at an election of directors, subject to limited exceptions. However, for issuers with a classified board of directors, the default approach is that directors may only be removed by the issuer's stockholders for cause. Under Delaware law, "cause" is generally limited to malfeasance in office, gross misconduct or neglect, false or fraudulent misrepresentations inducing the director's appointment, willful conversion of corporate funds, a breach of the obligation to make full disclosure, incompetency, gross inefficiency and moral turpitude. Typically, where stockholders are permitted to remove a director, the removal must be approved by a supermajority of the outstanding voting shares of the issuer.

Director Removed Only for Cause

Voting Percentage Required to Remove Director for Cause



Prohibition on Cumulative Voting

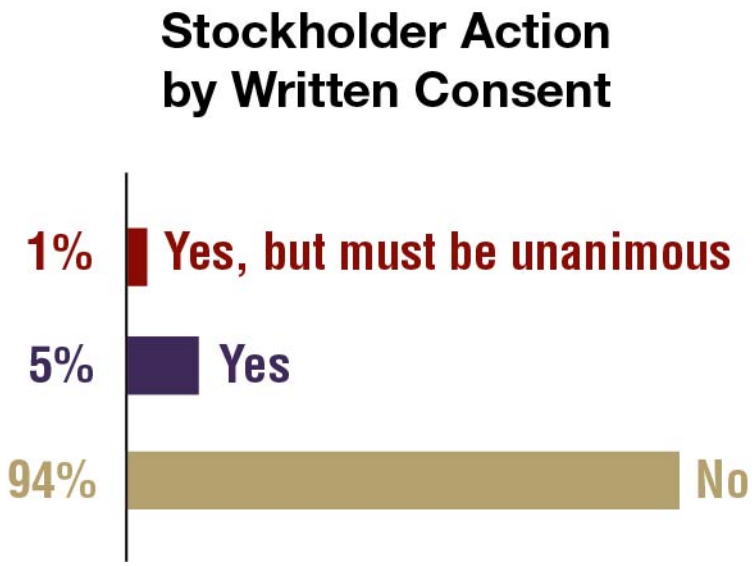
Cumulative voting is a method of election of the board of directors whereby a stockholder may cast as many votes for directors as the stockholder has shares of stock, multiplied by the number of directors to be elected. Under the cumulative voting method, a stockholder can elect to cast all of the stockholder's votes for one nominee, for example, which can allow minority stockholders of an issuer to achieve representation on the board of directors. In contrast, in "regular" or "statutory" voting, stockholders may not give more than one vote per share to any single nominee. Under the corporate laws of most states, including Delaware, an issuer may permit cumulative voting in the election of directors by providing for cumulative voting in its certificate of incorporation. None of the surveyed issuers permitted cumulative voting.

Prohibition on Cumulative Voting

Stockholder Action by Written Consent

Under the corporate laws of most states, including Delaware, stockholders are generally permitted to take action by written consent unless the issuer's governing documents provide otherwise. Stockholder actions by written consent are commonly used by private companies. If stockholders are not permitted to take action by written consent, then stockholders can only take action on proposals at an annual or special meeting of stockholders for which stockholders have been provided information about the matters to be voted on, and at which there is an opportunity to ask questions about the proposal. More than 20 proposals to permit stockholders to act by written consent were submitted to stockholder votes in each of 2012, 2013 and 2014 to date. Fewer than 30% of these proposals were approved each year.

As with many of the other defense measures, the prohibition on stockholder action by written consent is designed to encourage potential acquirors and other parties to negotiate with the issuer's board of directors prior to taking action. Among the six surveyed issuers that permitted stockholders to act by written consent, one required that the consent be unanimous for the stockholder consent to be effective.

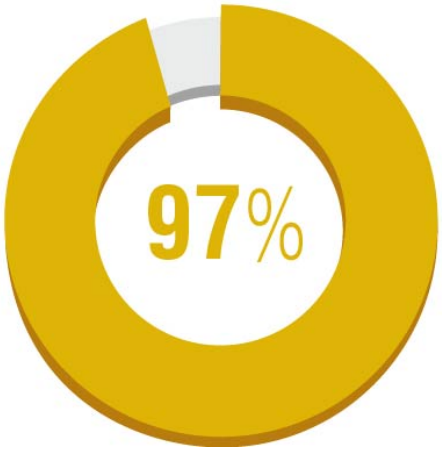


Stockholder Right to Call Special Meetings of Stockholders

Under the corporate laws of most states, including Delaware, an issuer can provide in its governing documents that the issuer's stockholders have the power to call special stockholder meetings. Absent special meetings of stockholders, actions that require stockholder approval can only be submitted for stockholder approval at the issuer's annual meeting of stockholders (unless stockholders are permitted to act by written consent). Therefore, special meetings can often be used by stockholders to effect corporate governance, board of directors and other changes at an issuer more expeditiously.

Among the surveyed issuers, 97% prohibited stockholders from calling special meetings. For these issuers, special meetings may only be called by the issuer's board of directors, the chairperson of the board of directors or the issuer's chief executive officer or president. For the three issuers that permitted stockholders to call special meetings, the minimum percentages of stockholders that must join in the request to call a special meeting were 10%, 25% and 25% of the outstanding shares entitled to vote. Two of these three issuers also limited stockholders' ability to call special meetings close in time to the issuer's annual meeting of stockholders. One of these issuers provided for dual class common stock (discussed below), and the right of stockholders to call special meetings will terminate if the class with superior voting rights is converted into the more junior class of common stock. At stockholder meetings in 2013 and 2014 to date in which stockholders voted on a proposal to permit stockholders to call special meetings, more than half of the proposals were approved.

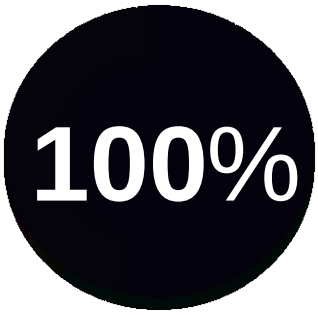
Prohibition on Stockholder Right to Call Special Meetings



Board Authority to Change Board Size

All of the surveyed issuers permitted the board of directors to change the authorized number of directors without stockholder approval. This allows boards of directors to unilaterally eliminate vacancies on the board of directors when a director resigns or is not reelected and allows boards of directors to create vacancies (which can usually be filled by the board of directors) at any time. Because issuers with a vacancy on the board of directors are at greater risk that a stockholder may submit a nominee for election to the board of directors, typically the number of authorized members of the board of directors equals the number of directors then serving on the board. Allowing the board of directors to determine its own size also prevents stockholders from packing the board of directors by increasing the size of the board and filling the newly created vacancies with stockholder designees.

Board Authority to Change Board Size



Board Authority to Fill Vacancies

All of the surveyed issuers permitted the board of directors to fill vacancies on the board of directors without stockholder approval.

Board Authority to Fill Vacancies

Majority vs. Plurality Voting in Director Elections

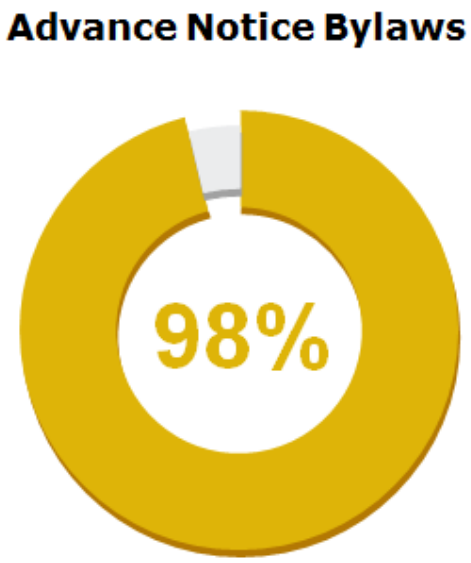
Under the corporate laws of most states, including Delaware, a director must generally be elected by a plurality of the votes; that is, the directors receiving the most votes for their election will be elected to the board of directors, regardless of whether the individual director receives more votes against his or her election than votes for his or her election. Under a plurality system, if the number of director nominees equals the number of available seats on the board of directors, each nominee only needs one "for" vote to be elected to the board of directors. However, an issuer can provide in its governing documents that directors are elected by a majority of the votes. There are a few variations of majority voting. Some require that the director nominee must receive a majority of the votes cast at the meeting in order for the director to be elected. Other standards require that the director receive a majority of the votes present at the meeting or a majority of the shares issued and outstanding. Under a majority voting system, if a director fails to receive majority approval, the nominee may need to immediately resign or submit a conditional notice of resignation, which is subject to acceptance by the board of directors (or its nominating committee).

The proxy advisory firms and a number of institutional stockholders favor majority voting in director elections. For those issuers that have adopted a majority voting standard, typically the voting structure changes to plurality in the case of contested elections where there are more director nominees than vacancies on the board of directors. Stockholder proposals to change from plurality voting to majority voting continue to be one of the most common proposals. In 2013 and 2014 to date, stockholder proposals to adopt majority voting were approved by stockholders in a majority of cases. Despite this, nearly all surveyed issuers adopted plurality voting for the election of directors.

Majority vs. Plurality Voting in Director Elections

Advance Notice Bylaws

Bylaws that include "advance notice" provisions require stockholders of the issuer to provide prior written notice to an issuer if the stockholder desires to nominate directors for election at a meeting of the stockholders or bring other business before a meeting of stockholders. Advance notice requirements are designed to provide an issuer's board of directors sufficient time to assess and respond to stockholder nominations and other proposals. In the case of director nominations, issuers generally require that the proposing stockholder provide detailed information regarding the director nominee, including the individual's principal occupation, experience and equity position in the issuer and other information that would be required to be disclosed in a proxy statement with respect to such nominee. Most advance notice provisions require stockholders to submit their proposals to the issuer between 90 and 120 days prior to the anniversary of the prior year's annual meeting of stockholders, subject to adjustment if the date of the annual meeting is more than 30 days prior to or following the one-year anniversary of the previous year's annual meeting stockholders. If a stockholder fails to comply with a validly-adopted advance notice provision, the issuer has the right to exclude the proposed matter from discussion or voting at the stockholder meeting.



Supermajority Voting and Percentage Required

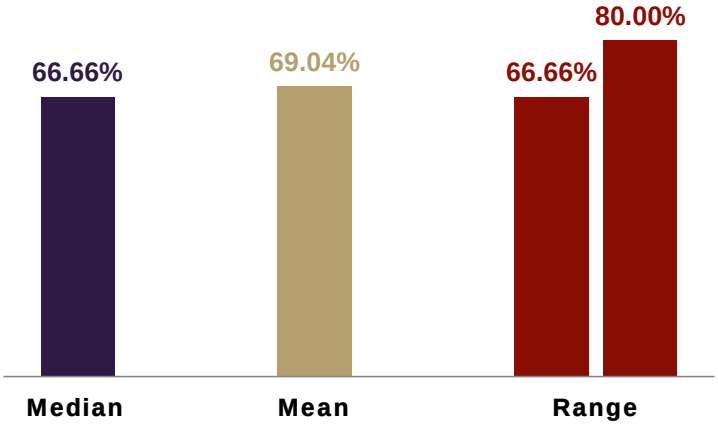
Under the corporate laws of most states, including Delaware, an issuer's stockholders generally have the power to amend the issuer's governing documents (*i.e.,* certificate of incorporation and bylaws) if the amendment is approved by a majority of the stockholders entitled to vote. However, an issuer can provide in its governing documents that greater than a simple majority of the shares entitled to vote is required to approve amendments to portions or all of the issuer's governing documents. Issuers typically adopt supermajority voting requirements with respect to the amendment or elimination of the issuer's defense measures contained in governing documents, including those discussed in this survey. This is designed to ensure that the issuer's protective mechanisms can only be eliminated or modified when it is clearly desired by a significant percentage of the issuer's stockholders. Because the supermajority voting thresholds are often tied to the outstanding number of shares entitled to vote in the election of directors, rather than the votes cast on a proposal or present at a meeting, it can be very difficult for stockholders to meet the supermajority requirement.

Stockholder proposals to eliminate supermajority voting requirements for amending the issuer's governing documents continue to be one of the most common proposals. In 2013 and 2014 to date, stockholder proposals to eliminate supermajority voting requirements were approved by stockholders in a majority of cases. In 2013, the proposal was passed at 16 of the 18 meetings at which it was proposed to stockholders for approval.

Most issuers that adopt supermajority voting requirements set the applicable voting threshold at 66.66% or 75% of the shares outstanding.

Supermajority Voting Required to Amend Governing Documents

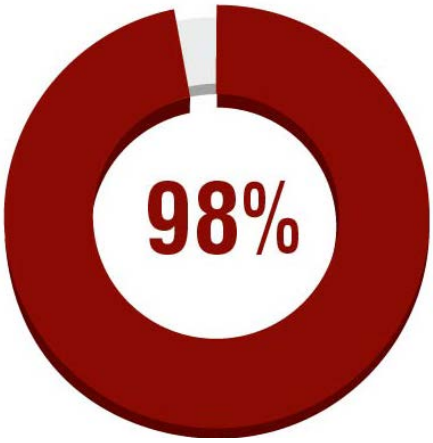
Supermajority Voting Percentage to Amend Governing Documents



Blank Check / Undesignated Preferred Stock

Nearly all of the surveyed issuers authorized blank check preferred stock, commonly referred to as "undesignated" preferred stock. Blank check preferred stock is authorized under the issuer's certificate of incorporation. Once authorized, the board of directors has the authority, without further stockholder approval, to establish the rights, preferences and privileges (e.g., voting, dividend and conversion rights) of one or more series of preferred stock issued by the issuer. These terms are typically set forth in a certificate of designation or certificate of amendment to the issuer's certificate of incorporation, which is filed with the secretary of state of the issuer's action prior to issuance of the preferred stock. Most issuers use blank check preferred stock for raising capital after the IPO, anti-takeover defenses, strategic transactions or a combination of the foregoing. Stockholder rights plans (discussed below) are typically created using the issuer's authorized blank check preferred stock. Issuers listed on Nasdaq or the NYSE must obtain stockholder approval to issue preferred stock representing, or convertible into, more than 20% of their pre-issuance common stock or voting power if the common stock equivalent purchase price of the securities is below the common stock market price or if the issuance would effect a change in control. Although blank check preferred stock is considered a defense mechanism, the usefulness of blank check preferred stock is generally acknowledged and accepted by proxy advisor groups and institutional stockholders.

Blank Check / Undesignated Preferred Stock



Stockholder Rights Plan / Poison Pill

A stockholder rights plan, commonly referred to as a "poison pill," is designed to deter unauthorized stock accumulations by imposing substantial dilution upon any stockholder that acquires shares in excess of a specified ownership threshold without prior approval from the issuer's board of directors. The ownership threshold typically ranges from 10% to 20%. A standard stockholder rights plan gives all stockholders other than the unwelcome acquiror or hostile bidder the right to buy additional stock (either in the target issuer or in the acquiror) at a substantial discount, which can significantly dilute the potential acquiror's economic and voting power. Stockholder rights plans are designed to force potential acquirors to negotiate directly with the target issuer's board of directors.

Proxy advisory groups, including ISS and Glass Lewis, disfavor the adoption of a stockholder rights plan without specific stockholder approval of the plan. ISS' voting policy on stockholder rights plans provides for a negative vote for directors at a newly public company that does not commit to placing its stockholder rights plan to a stockholder vote within twelve months following its IPO. Moreover, over the past few years, there has been a steady rise in the number of stockholder proposals seeking to repeal stockholder rights plans that either were not adopted with stockholder approval or have a term exceeding one year from the date of adoption.

Likely in light of the positions adopted by the proxy advisory firms and a number of institutional stockholders that invest in technology and life sciences IPOs, none of the surveyed issuers adopted a stockholder rights plan in connection with their IPO. Nonetheless, issuers that have authorized and unissued blank check (undesignated) preferred stock can quickly adopt a stockholder rights plan at any time after the IPO without obtaining stockholder approval.

Stockholder Rights Plan/ Poison Pill

NONE

Multi-Class Stock

Most issuers continue to go public with a single class of common stock that provides all stockholders the same per share voting and economic rights, with each share of common stock entitled to one vote. Under a multi-class structure, holders of one or more series of common stock are typically entitled to multiple votes per share and, in some cases, other rights not held by the issuer's stockholders generally. For issuers with a multi-class structure, the most "senior" series of common stock is generally held by the issuer's founders (or a subset of the founder group). The most "junior" series of stock is held by the issuer's other stockholders and is the series sold by the issuer in the IPO. Historically, multi-class structures were adopted predominately by family run businesses and media firms, including The New York Times Company, 21st Century Fox, News Corporation and Dow Jones & Co. More recently, we have seen multi-class structures adopted by a broader group of issuers, particularly by reputable technology companies whose founders continued to manage the issuer through and following the IPO, including Google, Facebook, LinkedIn and Zillow.

The multi-class structure generally provides designated stockholders with the ability to determine the outcome of matters submitted to stockholder vote. Proponents of this structure argue that it allows the issuer's managing founders to make decisions designed to serve the best interests of the issuer's stockholders over the long-term and focus on projects whose value may not be realized over the short-term or whose benefit may not be clearly obvious to the public markets. Some data suggests that issuers that adopt a multi-class common stock structure suffer a valuation discount compared to their peers with a single class of stock. The charters of some institutional stockholders prohibit these stockholders from investing in issuers with a multi-class common stock structure.

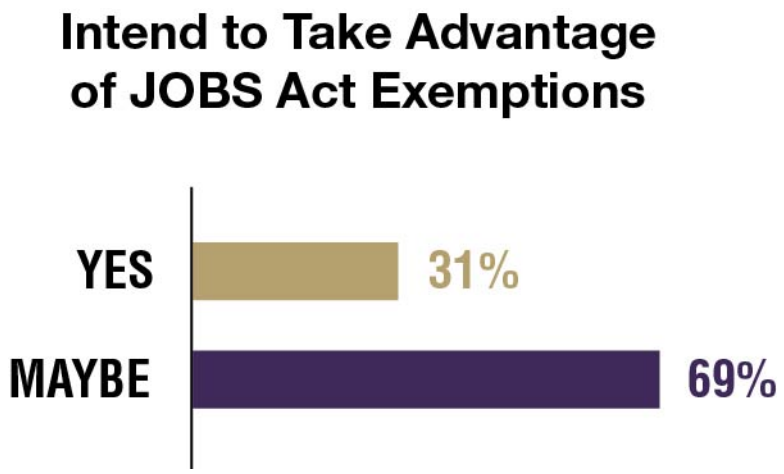
Dual Class Stock

7%

JOBS ACT PROVISIONS

Accommodations Generally

Each of the surveyed issuers provided some indication whether it intended to take advantage of one or more of the disclosure and compliance accommodations offered to EGCs under the JOBS Act. None of the surveyed issuers indicated that it did not intend to take advantage of any of these accommodations.



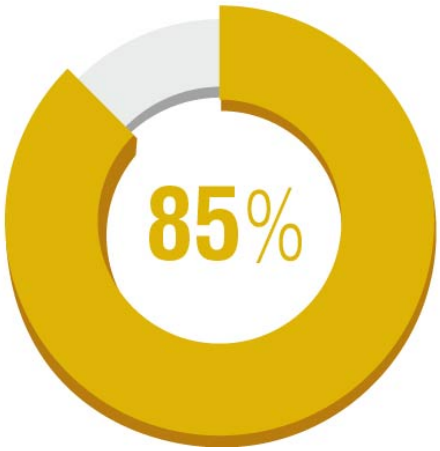
Confidential Submission

Nearly every surveyed issuer elected to submit at least one draft Registration Statement on Form S-1 on a confidential basis. In addition to allowing issuers to initially maintain the confidentiality of their IPO plans, draft registration statements impose fewer requirements than publicly filed Registration Statements on Form S-1. Specifically:

- draft registration statements are not required to be executed by the issuer, management or members of the board of directors;
- draft registration statements are not required to be accompanied by a consent from the issuer's independent registered public accounting firm or other experts;
- underwriters for the offering are not required to be specifically identified in the first draft of the registration statement;
- the issuer will not become subject to the Sarbanes-Oxley Act solely by virtue of submitting a draft registration statement; and
- the issuer is not required to pay the initial filing fees to the SEC when it submits a draft registration statement.

Issuers are required to make their first public Registration Statement on Form S-1 filing at least 21 days prior to the commencement of the road show for the IPO. Once the first public filing is made, all previously submitted draft registration statements for the offering are required to be "made public" on the SEC's EDGAR website to start the 21-day clock.

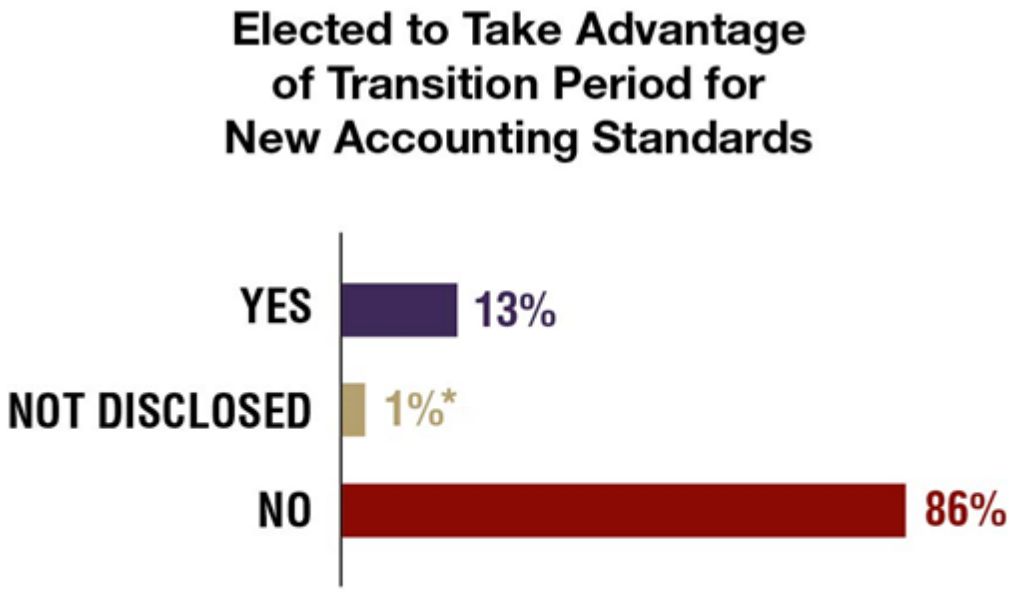
Confidential Submission



Compliance with New or Revised Accounting Standards

The JOBS Act provides that EGCs will not be required to comply with any new or revised financial accounting standards until those standards are also broadly applicable to private non-reporting companies (if they apply to such companies). However, EGCs are prohibited from choosing to apply some new or revised accounting standards and not others. Instead, they must opt in or opt out on a consistent basis. EGCs are required to disclose in their first submission or filing with the SEC whether the issuer is electing to opt out of the extended phase-in for new or revised accounting standards. An election to opt out is irrevocable.

EGCs that elect to use the extended transition period are required by the Staff of the SEC to include risk factor disclosure explaining this election and that, as a result of this election, the EGC's financial statements may not be comparable to issuers that comply with new or revised financial accounting standards at the time they are effective for public companies generally. The Staff of the SEC also typically requests that similar disclosure be included in the MD&A section of the issuer's prospectus.



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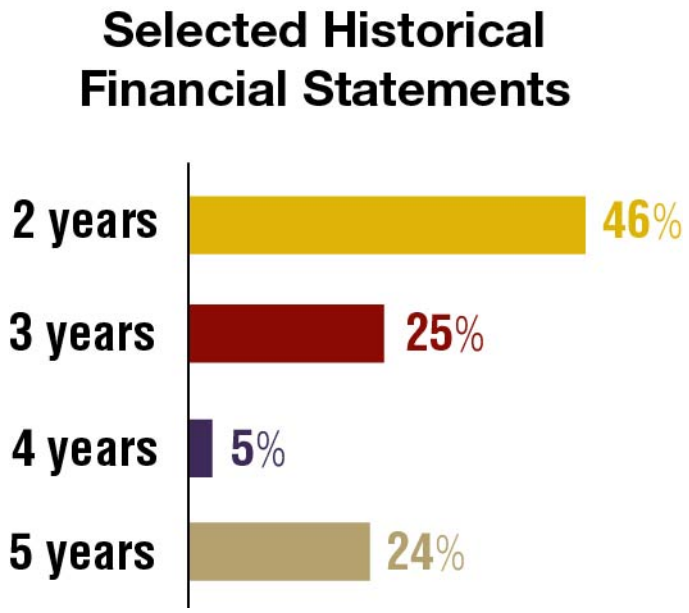
* Following the IPO, the issuer disclosed that it had irrevocably elected *not* to take advantage of the transition period.

Audited Financial Statements

Prior to the adoption of the JOBS Act, IPO issuers were required to include at least three years of audited financial statements in their IPO prospectuses. An EGC can provide two, rather than three, years of audited financial statements. A majority of the surveyed issuers elected to take advantage of the reduced requirements. The MD&A section of the prospectus is only required to cover the years for which the issuer provides audited financial statements, and any subsequent quarterly interim period. The ability to provide only two years of audited financial statements is a significant benefit to issuers that change their primary auditors just prior to commencing the IPO process.

Selected Financial Data

Prior to the adoption of the JOBS Act, IPO issuers were required to include up to five years of selected financial data in their IPO prospectuses. An EGC is only required to present selected financial data for periods corresponding to the audited financial statements contained in the prospectus. Therefore, issuers can present as few as two years of selected financial data. Some issuers voluntarily elect to include up to five years of selected financial data to show (positive) trends and allow for greater comparability of the issuer's financial performance to that of the issuer's peers and competitors. Surveyed issuers that included only two years of audited financial statements in their IPO prospectuses were far more likely to include less than five years of selected financial data.



Executive Compensation Disclosure

Under the JOBS Act, EGCs are permitted to take advantage of the scaled disclosure requirements available to smaller reporting companies (generally, companies with a public float of less than $75 million) with respect to executive compensation disclosures. In particular, EGCs may:

- omit the CD&A regarding executive officer compensation;
- provide compensation information for only three named executive officers (including the CEO), rather than five named executive officers; and
- provide only the following three of the seven compensation tables that are required to be provided by issuers that do not qualify as EGCs: Summary Compensation Table; Outstanding Equity Awards at Fiscal Year-End Table and Director Compensation Table.

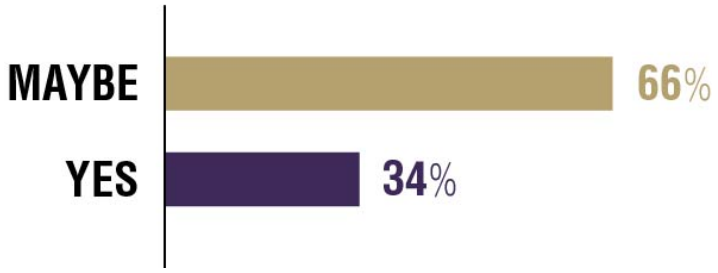
Most of the surveyed issuers elected to take advantage of all three of these accommodations available to EGCs.

Reduced Executive Compensation Disclosure

Internal Controls Audit

Under Section 404(b) of the Sarbanes-Oxley Act, issuers are required to provide an independent auditor attestation of management's assessment of the effectiveness of their internal control over financial reporting. Prior to the JOBS Act, all newly public issuers were able to delay compliance with this requirement until their second annual report on Form 10-K filed with the SEC, and public issuers that qualified as non-accelerated filers (generally, those issuers with less than $75 million of non-affiliate common equity market capitalization) were exempt from this requirement. EGCs are still required to maintain internal control over financial reporting and assess the effectiveness of their internal controls on an annual basis pursuant to Section 404(a) of the Sarbanes-Oxley Act beginning with the second annual report on Form 10-K filed after completion of the IPO. However, EGCs are not required to provide the independent auditor attestation under Section 404(b) of the Sarbanes-Oxley Act.

Intend to Omit Auditor Attestation under Section 404(b)

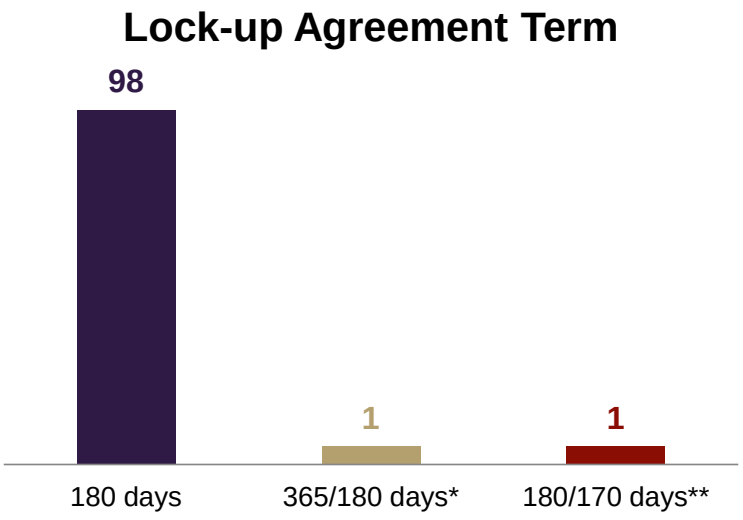


OTHER TERMS

Lock-up Agreements

Underwriters require that the holders of outstanding equity in the IPO issuer, as well as the issuer's insiders, to agree not to sell shares of the issuer's stock, including shares acquired as part of or following the IPO, for a specified period of time following the IPO without the underwriters' consent. Lock-up agreements also typically prohibit equityholders from exercising registration rights with respect to their shares. The purpose of lock-up agreements is to help maintain an orderly trading market in the issuer's stock during an initial period following the IPO. Without lock-up agreements, issuers (and underwriters) risk having a significant number of pre-IPO shares enter the market immediately after the IPO, which can place significant downward pressure on the issuer's stock price before the IPO shares come to rest.

The typical lock-up term is 180 days from either the pricing or the closing of the IPO. In certain circumstances, underwriters will demand a longer lock-up period for a subset of stockholders, including founders and holders of larger blocks of the issuer's post-IPO shares. The underwriters may also agree to a shorter lock-up period for some of the issuer's stockholders, but typically this is limited to those holders with extenuating circumstances or very small positions in the issuer's stock. On occasion, underwriters will agree to grant an early (staggered) release of the lock-up restrictions with respect to some or a portion of the shares held by the issuer's pre-IPO equityholders.



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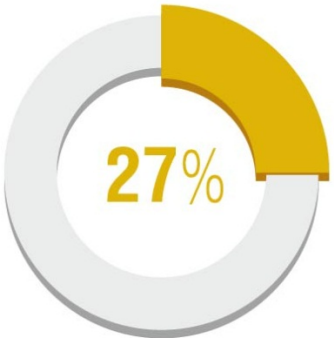
* Directors, executive officers and certain significant stockholders of the issuer were subject to a 365-day lock-up; the rest were subject to the shorter period.
** IPO selling stockholders and certain significant stockholders of the issuer were subject to a 180-day lock-up; the rest were subject to the shorter period.

Directed Share Program

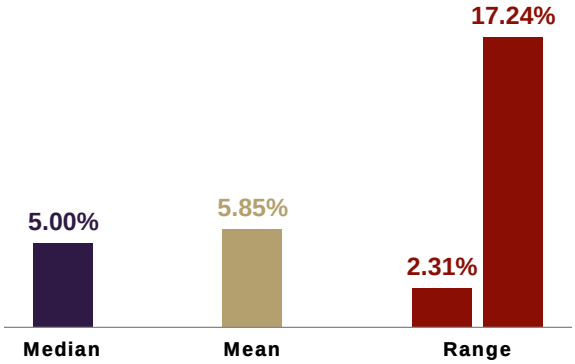
Under a directed share program, often called a "friends and family" program, the underwriters agree to set aside a percentage of the shares being sold in the IPO for sale to individuals designated by the issuer. These may include business associates, customers, vendors, directors, officers and employees and their family members that do not otherwise have the opportunity to purchase shares directly from the underwriters in the IPO. Under a directed share program, participants purchase IPO shares at the same price paid by the public IPO investors. In light of the anticipated post-IPO stock price appreciation, these programs can provide participants with potentially significant gains.

Although the issuer selects the individuals eligible to participate in a directed share program, the underwriters are typically responsible for administering the program. Underwriters typically require directed share program participants to enter into customary IPO lock-up agreements and to open a brokerage account with the underwriter managing the program (or one of its affiliates).

Directed Share Program



Directed Share Program Size
(as a percentage of initial/firm shares offered)



New Equity Incentive Plan

Nearly all of the surveyed issuers created a new equity incentive plan in connection with their IPO. These plans generally permit the issuer to issue a broad range of equity awards to employees and other service providers, including stock options, restricted stock awards, restricted stock units, stock appreciation rights, performance awards and deferred stock units, among others. Once the new equity incentive plan is adopted, all future equity awards granted by the issuer are made under the new equity incentive plan. Equity incentive plans must be approved by the issuer's board of directors and stockholders.

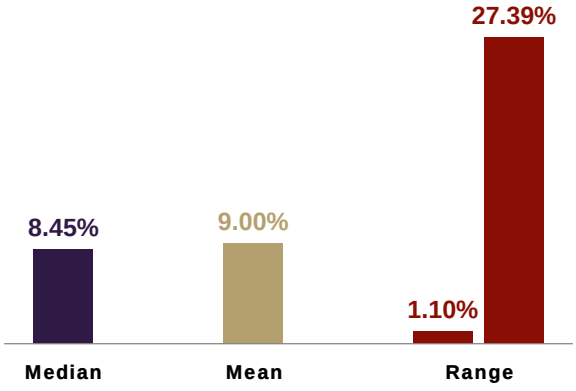
Issuers typically tie the number of shares reserved under the new equity incentive plan to the anticipated number of shares of common stock to be outstanding upon completion of the IPO. In most cases, shares subject to awards outstanding under the issuer's prior (i.e., pre-IPO) equity incentive plans that subsequently expire or are forfeited or cancelled are automatically added to the reserve of the new equity incentive plan.

"Evergreen" provisions provide for the automatic replenishment of an equity incentive plan's share reserve each year. Typically, the number of shares added to the reserve pursuant to the evergreen provision is either a pre-determined number of shares or based on a percentage of the shares of common stock outstanding immediately prior to the annual increase, in either case subject to the discretion of the issuer's board of directors (or its compensation committee) to select a fewer number of shares each year. The proxy advisory groups disfavor equity incentive plans with evergreen provisions. Therefore, IPO issuers that adopt a new equity incentive plan with an evergreen provision generally seek to obtain stockholder approval of the equity incentive plan prior to the IPO.

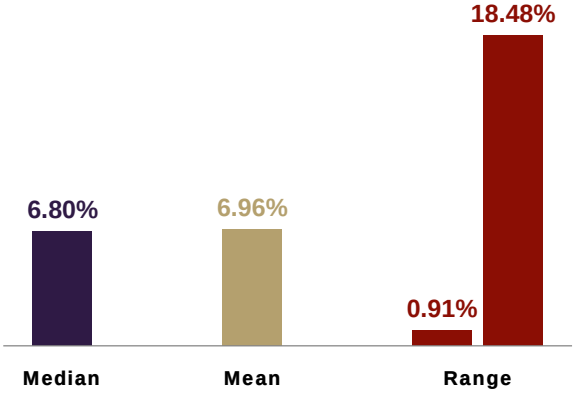
New Equity Incentive Plan

New Equity Incentive Plan (cont.)

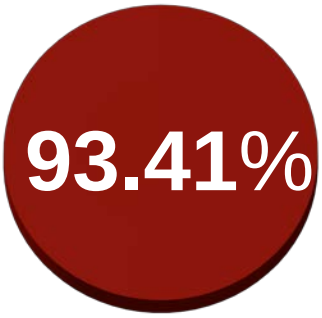
New Equity Incentive Plan Reserve (As a percentage of actual post-IPO shares outstanding)



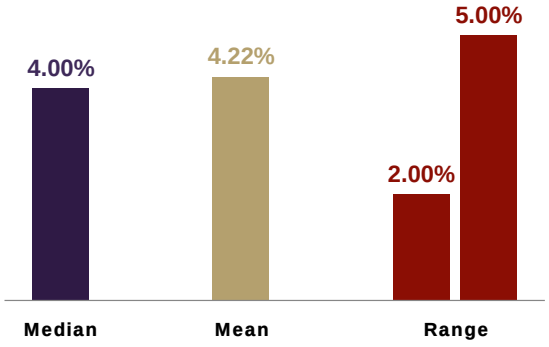
New Equity Incentive Plan Reserve (As a percentage of fully-diluted post-IPO shares outstanding)



New Equity Incentive Plan with Evergreen



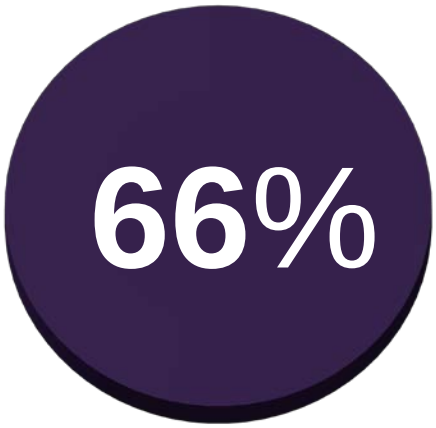
New Equity Incentive Plan Evergreen Percentage Increase / Year



Employee Stock Purchase Plan

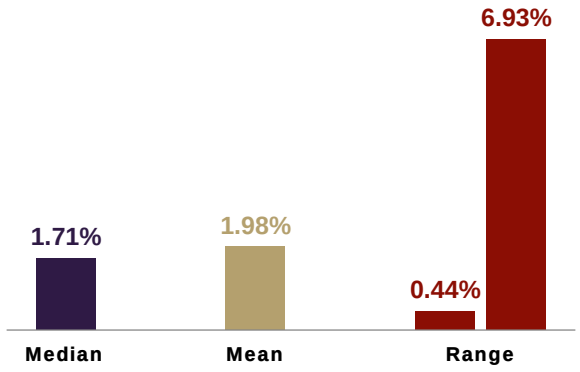
An employee stock purchase plan (ESPP) is an issuer-sponsored plan that permits employees of the issuer to use after-tax payroll deductions to purchase the issuer's common stock, often at a discount from the market price, at the end of specific purchase periods. The purpose of an ESPP is to encourage broad-based employee ownership of employer stock. These plans are typically adopted to supplement, and not replace, the issuer's equity incentive plan.

New ESPP

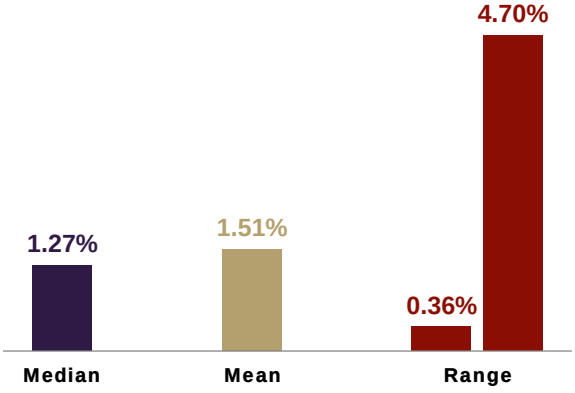


Employee Stock Purchase Plan (cont.)

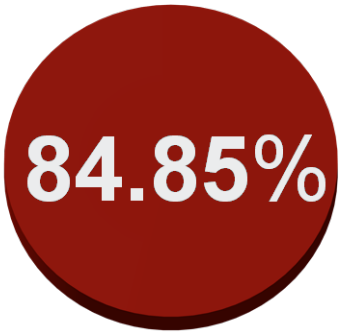
New ESPP Reserve (As a percentage of actual post-IPO shares outstanding)



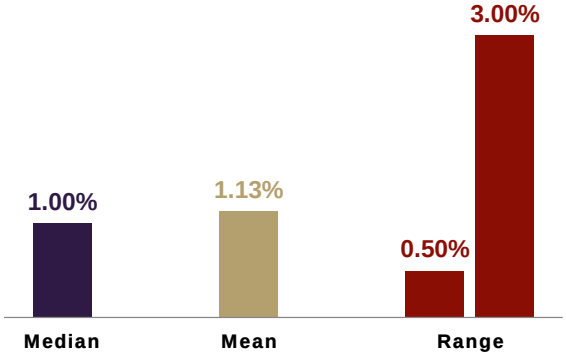
New ESPP Reserve (As a percentage of fully-diluted post-IPO shares outstanding)



New ESPP with Evergreen



New ESPP Evergreen Percentage Increase / Year



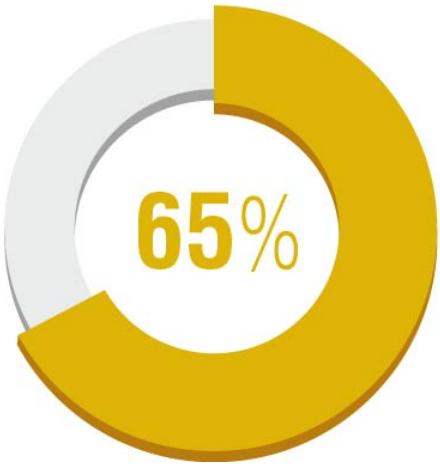
Forum Selection

Forum selection clauses typically provide that a certain jurisdiction (e.g., the issuer's state of incorporation), a certain court within a specified jurisdiction, or both, shall be the sole and exclusive forum for bringing and adjudicating specified actions or proceedings. The types of matters covered by the provision generally include stockholder derivative actions, claims by stockholders alleging a breach of fiduciary duty against the issuer or its directors or officers, claims arising under the corporate laws of the issuer's state of incorporation or under the issuer's governing documents, other similar actions or suits brought by the issuer's stockholders and, with respect to some jurisdictions, any action asserting a claim governed by the internal affairs doctrine.

The adoption of exclusive forum provisions by public issuers increased substantially following a decision of the Delaware Court of Chancery in March 2010, which noted in dicta that "if boards of directors and stockholders believe that a particular forum would provide an efficient and value-promoting locus for dispute resolution, then corporations are free to respond with charter provisions selecting an exclusive forum for intra-entity disputes." In July 2013, the Delaware Court of Chancery upheld the validity of exclusive forum bylaws unilaterally adopted by an issuer's board of directors.

Exclusive forum provisions are contained either in the issuer's certificate of incorporation, the issuer's bylaws or both. Although the addition of exclusive forum provisions to bylaws requires board of directors, but not necessarily stockholder, approval, these provisions cannot be added to a certificate of incorporation without the approval of both the board of directors and stockholders.

Issuers with a Forum Selection Clause



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Authors and Acknowledgments

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