

Preparing for an IPO: A Board Member's Perspective

As mid-2024 economic conditions continue to prove challenging, companies with Initial Public Offering (IPO) aspirations are anticipating the 2025 window — with some eyeing late 2024 if conditions improve — and taking critical actions in preparation.

The transition from private to public represents a pivotal moment for any company and brings increased workloads, complexity and scrutiny. In the first of a three-part series, Aon's Executive and Board Advisory practice offers a checklist of key steps and best practices for compensation planning in the 12+ months leading up to IPO. Future pieces will offer guidance on how to avoid common equity overhang and governance policy pitfalls and considerations for transitioning director compensation.

Given the complexity of the IPO planning process, management teams and board members should begin compensation planning far ahead of the expected IPO date, ideally 12 to 18 months prior to the intended transaction date. A company's talent strategy plays a critical role in ensuring the company is ready to grow, hire and retain the key staff needed for the next phase of growth and success. More specifically, pay strategy and policies can be used as a key differentiator when designed to fit a company's culture — and not simply following market trends.

Preparing for an IPO requires a thorough review of all compensation policies, including executive and director compensation, and extending to non-executive employees (including sales). A lack of pre-IPO awareness and planning around compensation-related topics will result in opportunities lost, particularly for companies reliant on equity compensation as a differentiator.

Board members should consider the following steps to effectively manage the planning process leading up to IPO:

- Establish and adhere to an IPO checklist covering the key compensation and equity-related issues to consider in planning (see below for a sample template).
- Design a new equity plan aligned with market practices and company strategy, right-size the new share pool request, and implement key design features.

IPO Runway and Checklist:

12+ Months Before IPO*

Compensation Committee:

- Establish draft annual compensation committee calendar/charter
- Conduct pre-IPO education for committee and senior management to address needed shift in mindset from private to public
- Clarify roles for HR, CEO, CC Chair and Independent advisors

*Assumes first filing of Form S-1 approximately 3-4 months pre-IPO

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9 Months Before IPO*

Peer Group:

- Develop appropriate peer group of 15-25 similar public companies to assess executive/board compensation practices
- Key peer selection criteria include industry, business profile, revenue, market cap, profitability, headcount, risk profile, debt leverage, time since IPO, and other key company-aligned metrics

Compensation Philosophy:

- Develop pay philosophy and transition strategy to migrate programs from private to public practices
- Many companies choose to align executive cash near the marketplace 50th percentile at the time of IPO

6 Months Before IPO*

Executive Compensation for IPO:

- Assess executive compensation program relative to approved post-IPO market to determine adjustments
- Ensure cash programs for both executives and board members are competitive with the public marketplace. This is key for the retention of employees and recruitment of new executives and board members

Equity Ownership and Retention Value:

- Assess equity holdings and value for employees to determine if any adjustment or refresh grants should be considered prior to IPO
- Note: The timing of the first public equity grant will depend on a variety of factors, including IPO timing and if any grant action was taken in conjunction with the IPO

Cash Incentives:

- Review short-term incentive program(s) and align with public market practices

Equity Strategy and Guidelines:

- Review/design equity strategy and guidelines for the pre- and post-IPO environment (for broader employee population)
- Note: Ensure the equity plan allows for the types of compensation and programs that align with the company's long-term strategic goals, in addition to comparing compensation levels and targets across peers
- Note: It is generally easier to obtain approval for new plans or modifications for existing plans while the company is still privately held

Equity and ESPP Funding:

- Determine funding for post-IPO equity plans, including evergreen provision and Employee Stock Purchase Plan (ESPP)

Board Compensation:

- Implement board of director compensation program consistent with public company market practices

S-1 Compensation Disclosures:

- Draft/review a Compensation Discussion & Analysis (CD&A), if required, to be filed as part of Form S-1 Prospectus

Governance/Risk:

- Assess potential risks in all compensation programs, particularly for key employees, and provide guidance on key corporate governance and investor issues

3 Months Before IPO*

Executive Contracts and Termination Protection:

- Review executive severance and change-in-control protections for consistency with public market and governance best practices

*Assumes first filing of Form S-1 approximately 3-4 months pre-IPO

Compensation drives the ability to attract and retain talent in a competitive marketplace. Given the importance of these decisions in the public realm, careful planning and decision-making is important leading to IPO. Adequate education of the Board and senior leadership on these issues, including the heightened expectations in the public realm, will enable the company to hit the ground running upon the completion of the IPO.

The next two articles of this three-part series will discuss related considerations for boards and leadership teams transitioning from private to public.

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