



G U N D E R S O N D E T T M E R

IPO READINESS: SETTING THE STAGE FOR A SUCCESSFUL IPO PROCESS

2024





INTRODUCTION

The key to a successful IPO is early preparation. For most companies considering an IPO, this preparation starts 18 months to two years before the IPO launches. Late-stage private companies that begin working towards IPO readiness early will be well-positioned to execute an IPO and to thrive as a public company. This guide focuses on the pivotal 18-month period before the organizational (“org”) meeting with the full IPO working group and provides an overview of key gating items, timelines, and public company considerations that in-house counsel should consider along the way.

The IPO process typically takes five to six months from the org meeting to the closing of the IPO, and rigorous preparatory work will reduce the strain on management during that time.

Companies looking to this guide should consider their individual circumstances when prioritizing the various items we have highlighted. For example, a tech unicorn developing AI technologies may have quite different pre-IPO concerns than a biotech company developing precision oncology drug candidates, even if both companies are planning to go public in the same timeframe.

This guide focuses on traditional IPOs and not on other paths to becoming publicly listed (such as via a direct listing, de-SPAC transaction, or reverse merger). Nevertheless, companies face many of the same public-company readiness considerations regardless of their path to listing.

Below is an abbreviated timeline showing the various areas of focus for IPO readiness during the 18-24 months prior to the IPO:

Start of IPO Preparation		Org Meeting		IPO
18 to 24 Months Before IPO		12 to 18 Months Before IPO		6 to 12 Months Before IPO
Auditing and Accounting Matters		Governance		Prepare for IPO Diligence
Board Matters		Updates to Policies, Processes and Systems		Refine the Business Story
Team Composition				S-1 Preparation
Equity Compensation				Equity Compensation
				Communications
				Investment Bankers and Analysts
				Diligence
				Testing-the-Waters Meetings
				SEC Filings and SEC Review
				Roadshow
				Pricing and Closing of the IPO

18-24 MONTHS PRE-IPO

Auditing and accounting matters

Audited annual financial statements. To complete an IPO, companies will need either two or three years of financial statements audited at the PCAOB-level by an independent registered public accounting firm. The completion of these audits is often the biggest gating item for an IPO. Late-stage companies should consider whether they have auditors appropriate for a public company or whether a change is needed. Many companies are surprised to discover that, even if they completed audits as a private company, a public company audit by a “Big 4” accounting firm (and review by the auditor’s “national office”) often result in significant and time consuming accounting issues that need to be resolved prior to submitting a Form S-1 to the SEC. Companies should also consider doing a dry run of a PCAOB-level audit at least one fiscal year before beginning the IPO process. Getting audits done early in the process will help alert the company to any pain points that need to be addressed.

Quarterly and interim financial statements. In many cases, companies choose to include financial information for each of the trailing eight quarters in the IPO S-1 to help illustrate trends, demonstrate seasonality and generally “tell their story” during the IPO. Underwriters often view this quarterly information to be helpful for the marketing process, but request that this additional quarterly information undergo audit review procedures by the company’s auditors. Timing can be an issue for this information, particularly if a company’s accounting/finance team is not accustomed to preparing it. In addition to this quarterly financial information, depending on deal timing, companies may be required to prepare interim financial statements to comply with SEC rules (e.g., for the six months ended June 30 or the nine months ended September 30), which would be subject to audit review procedures by the company’s auditors. Often, a company will need to grapple with issues related to retroactively applying a quarterly close process, as well as drafting footnotes to quarterly financial statements.

Acquisitions. SEC rules might require separate stand-alone audited financial statements of recently acquired companies or where an acquisition is probable (even if it has not closed), if the acquired company’s financial statements are deemed to be “significant” in comparison to the acquiror’s financial statements. Companies that have made, or are considering, acquisitions should review the Regulation S-X significance tests with their auditors. These significance formulas are not intuitive and obtaining stand-alone audited financial statements for the acquired business(es), as well as unaudited pro forma financial information, could be burdensome (or require the company to undergo a waiver process with the SEC).

Board matters

General. When a company transitions from a private company to a public company, its corporate governance must undergo significant changes. Whereas the role of a board of a private, venture-backed company typically involves supporting the founders in achieving their vision and strategically advising them along the way, a public company board is required to step up its oversight and risk management role. The earlier that a board is accustomed to addressing these new roles, the easier it will be to transition to public company life.

Skills and independence. SEC and stock exchange rules generally require listed companies to have a majority-independent board and fully independent committees. “Independence” means that a board member can act in the best interest of the stockholders without being unduly influenced by management. It can take time to locate independent directors who are appropriately qualified to join the company’s board. SEC and stock exchange rules also require that at least one audit committee member qualify as a “financial expert,” and directors with this expertise are in very high demand. While there are post-IPO phase-in periods for these rules, the lack of a majority-independent board or fully-independent committees could prompt questions from investors during the IPO process. Accordingly, underwriters will typically push a company to be fully in compliance with the independence requirements at the time of the IPO.

Diversity. While the future of state law board diversity requirements is uncertain, certain underwriters will not take companies public unless their boards meet minimum gender, racial or ethnic diversity thresholds. Additionally, Nasdaq requires disclosure of board diversity, and SEC rules on board diversity disclosure are expected in the near term. In addition, although proxy advisory firms do not typically influence the execution of an IPO, these firms will generally recommend voting against certain directors serving on insufficiently diverse public-company boards at post-IPO annual shareholder meetings.

Committees. Companies that do not already have public-company-style committees in place (i.e., audit, nominating/governance, and compensation) should consider implementing one or more of those committees now, together with a committee charter that adheres to best practices for late-stage companies. This will provide helpful preparation for the board, executives, and legal team, particularly for companies that have not yet established a cadence of quarterly board and committee meetings.

Risk management. Public company boards are expected to oversee the company’s enterprise risk management. Accordingly, prior to an IPO, the board should implement systems and procedures to facilitate their oversight of the company’s risk. This entails a periodic exercise for management to report to the board on the company’s most pertinent risks, assessing the magnitude of those risks and addressing risk mitigation.

Team composition

Senior management. It is critical that the right management team is in place, and has had sufficient time to develop a track record, before beginning the IPO process. The board should consider whether any new hires are needed (such as a CFO with public company experience).

Other critical roles. Beyond the board and C-suite, hiring experienced finance, accounting, SEC reporting, equity administration, and investor relations personnel prior to the IPO will be helpful during the IPO process, help ease the transition into public company life, and decrease the likelihood of Sarbanes Oxley Act (“SOX”) or other internal/disclosure controls issues. This team will play a central role in preparing public filings in the future. Moreover, public companies will need to have adequate financial and accounting personnel so that quarterly results can be prepared and reviewed on the SEC’s reporting schedule.

Equity compensation. Consider transitioning to a quarterly cadence for obtaining independent appraisals of the fair market value of the company’s common stock, to help ensure that all equity awards are granted in compliance with Section 409A of the Internal Revenue Code. Be sure that all equity awards are granted pursuant to an appropriate securities law exemption (such as Rule 701), and be wary of any limitations or disclosure obligations triggered by these awards. The SEC will scrutinize a company’s prior equity award grants as part of the IPO process.

12-18 MONTHS PRE-IPO

Governance

Post-IPO, the company’s shareholder base and its relationship with its shareholders will be quite different than they were before. To help prepare for this transition, companies should consider:

- **Multi-class share structure.** These structures are very common in tech IPOs, particularly where a founder or founder group wants to retain voting control, and have generally been accepted by the market. The company will need to consider which pre-IPO shareholders will get “high-vote” stock, and how long that structure will remain in place. To the extent the company will be a “controlled company” after the IPO, this will implicate additional governance decisions. Proxy advisory firms and institutional investors do not generally oppose multi-class share structures so long as they have a reasonable sunset period (e.g., 7 years from IPO).
- **Anti-takeover protections.** It is common for companies, and important for companies with single-class share structures, to implement anti-takeover provisions in their governing documents before the IPO. It is much more difficult to implement these provisions once the company is public. In addition to multi-class share structures, these protections can include prohibiting stockholder action by written consent; implementing a classified board; permitting director removal only for cause; allowing only the board to fill director vacancies; and providing for “blank check” preferred stock, among others.

Updates to policies, processes and systems

Document management and internal controls. To prepare for IPO diligence, companies should begin gathering and maintaining a database of their historical corporate records, including their board minutes, stockholder actions and material contracts. In addition, consider obtaining tools for the following functions (and/or upgrades or improvements to current systems, if applicable): board management software; '34 Act and Section 16 reporting capabilities, and stock administration, along with the appropriate personnel and training to utilize these tools. Consider engaging a SOX readiness firm to develop a compliance roadmap and perform risk assessments and controls testing.

Governance updates. The company should have visibility into post-IPO board membership before kicking off the IPO process. In addition to assessing whether new directors are needed (as discussed above), companies should discuss with board members whether they plan to stay on the board after the IPO, and which members will join which post-IPO board committees. The board will need to adopt public-company committee charters in connection with the IPO, as well as various public-company policies (such as governance guidelines, a code of ethics, an insider trading policy, a whistleblower policy and a clawback policy). It is important to have the right directors in place to provide meaningful input on these documents and processes.

In addition, the SEC and investors continue to be focused on human capital and ESG issues. As a result, companies should be prepared to disclose and discuss their approaches to human capital and sustainability matters that are relevant to the business. The SEC adopted climate change disclosure rules in March 2024 (though such rules are currently stayed pending the resolution of litigation) and has identified 2024 as its target for proposing human capital disclosure rules.

Communications and metrics. Some late-stage companies choose to publish quarterly "earnings releases" beginning about a year before kicking off the IPO process. If desired, this can help a company establish a usual practice that may enable it to continue providing factual, historical information about the business during the IPO "quiet period". Even for companies that do not plan to externally publish these releases, preparing a quarterly release can help the company begin to hone in on its key reportable metrics, and get in the practice of consistent reporting.

6-12 MONTHS PRE-IPO

Prepare for IPO diligence

The IPO diligence process is intensive because it underpins the preparation of the S-1 registration statement, which is the document filed with the SEC during the IPO process. Underwriters will generally request records for at least the past three fiscal years. Understanding the scope of this process and considering whether any material contracts will need to be filed with the SEC (and if so, whether any sensitive information in those contracts needs to be redacted via a confidential treatment process with

the SEC and coordination with the contract counterparty), are all workstreams that the company should begin considering prior to kicking off the IPO process.

In addition to gathering historical records for the last few years, and participating on diligence calls with the IPO working group once the IPO process kicks off, the company will need to provide “back-up” files for all material operating or statistical data (other than financial information) included in the S-1. This can be time-consuming and require coordination across different areas of the company. In addition, underwriters may ask to hold diligence calls with a company’s customers or partners.

This is also the time to take corporate “clean-up” actions, such as finalizing board minutes and obtaining necessary approvals or ratifications from the board or existing stockholders on matters that may not have been adequately documented.

Every company will have issues that arise during diligence—this is normal. The point is to identify these issues early, and devise a strategy to address them. Accordingly, it may be helpful to review a typical list of underwriter’s diligence questions (e.g., cybersecurity, regulatory, IP, legal) so that the company can identify potential areas of weakness that can be addressed prior to the IPO kick-off.

Refine the business story

How the company presents its business in the IPO S-1 should be consistent with how management plans to talk about the business on an ongoing basis (both to the street and to business partners). What are the company’s greatest strengths? What are its top growth strategies? How do the company’s solutions address market needs? If a late-stage company has a history of releasing financial information, then the S-1 will need to pick up and continue that story. The underwriters will assist in positioning the company to address areas of investor interest and to anticipate investor questions, but the plotline of the story should come from management.

Biotech companies should consider what data will read out before or during the IPO process and the cadence of future data readouts. In addition, biotech companies should consider the timing of their various clinical development milestones. Investors and securities analysts will pay close attention to this information.

Thought should also be given as to whether any non-GAAP financial measures are important to an understanding of the business, what its key performance indicators (“KPIs”) are, and whether segment reporting will be required. The SEC’s stated goal for performance metrics disclosure is to help investors to see the company “through the eyes of management.” The company should generally be prepared to publicly report, on a quarterly and/or annual basis, the KPIs that it includes in the IPO S-1.

S-1 preparation

Business description. Assess internal bandwidth to help with early S-1 preparation. If the company is fairly certain it will proceed with an IPO in the near term, consider sketching out key sections of the disclosure before the org meeting. It can be helpful to refer to the company's "investor deck" as part of this drafting process and management should review the disclosures of comparable public companies. Consider hiring an IPO prep firm to support drafting and other workstreams. Note, however, that overreliance on a consultant during the IPO process can be challenging from a go-forward perspective. The company should also consider which functional areas should be included in discussions around business disclosure. Once the company is public, this group will be responsible for ensuring that public disclosures about the business remain current.

Financial information. SEC rules dictate which financial statements are required in the S-1 and when they must be updated. Once companies and their advisors develop a timeline for executing an IPO, they can determine which financial statements they will need at the beginning and which they will likely need at the end of the process. In conjunction with preparing the financial statements, the finance and accounting team will take the lead on preparing KPIs and non-GAAP information as well as accompanying narrative disclosure in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section, known as MD&A. This disclosure is intended to allow investors to see the company "through the eyes of management." The narrative cannot simply recite differences in line items; rather, MD&A is required to describe known trends and uncertainties and to quantify the effects of drivers on financial changes. In general, the MD&A from the S-1 will set up the framework for how the company prepares its financial disclosures in its future quarterly and annual reports.

Risk factors and other sections. Company counsel often uses company records to write the first draft of sections other than the business description, which will then be reviewed by management. It is critical that management and the legal team devote adequate time and attention to the risk factor disclosure in the IPO S-1, so that it accurately reflects the material risks to the business and is tailored to the company. (This is the cheapest "insurance policy" against post-offering litigation.) This disclosure should provide meaningful discussion of often scary risks without including talking points that hurt the business and sales teams (or create a roadmap to litigation). It is also critical that any risk factors that are drafted using solely hypothetical language have not actually occurred – the SEC has been very focused on this, most notably in the context of cybersecurity incidents.

Equity compensation

Post-public equity compensation program. Identify executive officers and Section 16 officers and assess changes to compensation and underlying documentation. Consider engaging a compensation consultant early in the process, who can help the company benchmark against its public peers and recommend an appropriate equity pool and other compensation parameters in light of the company's needs and goals. Compensation programs should be designed so that investors can see how they

promote the execution and achievement of the company's strategy. Many companies will be required to take an annual stockholder vote on executive compensation on an advisory basis. In addition, consider a new equity administration platform to support the company once it is public.

Pre-IPO grants. Consider how to address any RSUs or options nearing their expiration, especially in the event of a delay in the offering. Identify whether a large number of employee RSUs will vest upon the IPO's closing and work with the underwriters, counsel and the equity administration team to make sure the company is positioned from both a disclosure and execution position to handle tax withholding obligations. If any large equity grants to management are expected late in the IPO process, be aware that this can give rise to complicated "cheap stock" questions and review cycles with the SEC during the comment letter process. In addition, loans to executive officers, including those made to support early option exercises, will need to be repaid before the IPO can be completed.

Communications. The company's internal and external communications practices will likely need to evolve to reflect public-company considerations that require more discretion around what the company says, when and to whom. Public companies, for example, typically implement policies relating to insider trading and Regulation Fair Disclosure, known as Reg FD. Consider starting this transition following the org meeting, when the company will be headed into the IPO "quiet period". In particular, update the company's external communications policies (which should cover social media), and consider tightening up disclosure practices if they include disseminating news internally or to selective third parties.

The company should also consider conducting timely quarterly closes and mock earnings calls in advance of going public, to build "muscle memory" around the process and identify any pain points. Holding mock earnings calls with existing stockholders can give management a productive forum to fine-tune its planned post-IPO earnings messaging, as many late-stage private companies already have "cross-over" funds or other experienced public company investors on their cap table. While forecasts will not be shared in the IPO S-1, the company's ability to forecast and project earnings will be an important part of building analyst models and providing quarterly and/or annual guidance as a public company.

Investment bankers and analysts. In a traditional IPO, investment bankers help companies position themselves in the market and build a market for the shares being offered. It is important to identify bankers that deeply understand market conditions as well as the company's business and industry. In addition, this is the time to think about the group of analysts that a company would want to have cover the business after the IPO. Many late-stage companies hold analyst days ahead of their IPOs (in coordination with the IPO underwriters) to help financial analysts understand their businesses when the IPO is launched. Engaging with investment banks early in the process affords the opportunity to "road test" their capabilities and to build a relationship. For example, working with the investment banks to prepare/refine the company's investor deck for non-deal roadshows or testing the waters meetings with investors will reveal a lot of information about the banking team's industry perspective and dedication to the company.



We maintain an active practice representing our clients in their path to going public and as public companies after their initial listings.

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