Trends Around Director Compensation in Pre-IPO Companies

Introduction

Whether you are a boardroom veteran or just starting to dip your toes into directorship, finding accurate data on compensation packages for incoming directors is always helpful. Compensation data at private companies, especially those in the pre-IPO stage, may be difficult to pin down thanks to the wide spectrum of pay practices among younger, private enterprises and the inherent uncertainty of the IPO process. Understanding the pay landscape, however, offers incoming directors powerful knowledge that can be used to shape negotiations and ensure they are making the right decisions about which boards to join, and when.

The following article provides an in-depth look at the typical ranges seen in today's director pay packages, actionable advice you can use to steer compensation discussions, and a series of deeper questions and considerations derived from Semler Brossy's experience in similar negotiations. While the primary focus will be on companies with a runway to IPO, the information may provide valuable context for anyone considering a position as a board director in the near future.

The Basics of Director Compensation: Understanding Your Leverage

Compensation packages for incoming directors at private companies generally consist of Restricted Stock Units (RSUs), stock options, or some combination of the two. They are frequently front-loaded equity grants meant to cover multiple years, as opposed to the annual grants common in public companies. In order to get a better idea of the landscape, Semler Brossy analyzed 36 pre-IPO awards granted between 2015-2020 at high profile tech companies who hired non-chair, independent director(s) twelve months prior to IPO. In general, we found that these grants are usually coupled with a 3-4-year vesting period, and more than half of them also require an actual IPO for vesting (known as an "IPO Trigger"). Compensation is almost entirely equity based—of the 20 pre-IPO companies studied, only two offered any direct cash pay—which is typical for pre-IPO companies.

Broadly speaking, incoming directors have the most negotiating power early in the IPO process, typically the B or C-series round of capital formation. As the IPO becomes imminent, the chances that you will be offered a package that is similar, if not identical, to the rest of the board increases meaningfully. Time, however, is not the only factor at play during negotiations. A variety of factors, as seen in the following table, will help determine how much leverage you may have in shaping your pay package.

Increases Negotiating Power	Decreases Negotiating Power
First / only director being hired	Multiple directors hired at the same time
Higher Levels of Risk (long timeline to IPO, early stage uncertainty, liquidity risk)	Less Risk or Uncertainty (closer to IPO, strong valuation)
Unique or essential skills needed by board	Board largely established / no unique skill gaps
"Deal Making" or idiosyncratic founder personality	High level of board / corporate stability or orthodoxy
High-profile background or connections	Less experience with boards / governance

Navigating the Pre-IPO Runway: What to Expect at Each Stage

As previously alluded to, the most significant factor determining the value and structure of a director's pay package is the amount of time until IPO. While the three stages outlined below are not hard and fast timeframes, there are some significant differences between the compensation structures of early, mid-stage, and soon-to-IPO companies worth considering. Accordingly, each stage offers prospective directors varying degrees of flexibility, risk, and opportunity.

Stage 1—The First Director (>36 months to IPO)

The early bird gets the worm or, in this case, the best shot at dictating the worm's terms. Around the B or C-series round of fundraising, companies will typically begin looking to hire their first director who is not an employee nor affiliated with an investor. This person plays a key role in guiding management during the high-risk, early stages of the company, and the role requires a host of crucial fiduciary responsibilities regarding future investors. As a result, the first director is typically granted the greatest leeway in compensation negotiations. Because they are taking on the highest risk and have the longest time horizon on payout, earlier directors typically have higher economic value than newer additions.

That said, these awards still tend to stick close to the common structure: a large, 4-year vested equity grant meant to cover multiple years. We tend to see a higher percentage of stock options at this stage. These shares are often valued as a percentage of the company, frequently at 20-50bps of the organization.

This can grow even higher, however, if the company is smaller, in a very nascent stage, or is considering bringing the director on as Board Chair. While this range is relatively standard, we have seen some as high as 1%. Generally, we see no promise of additional compensation or refresh awards down the line, though additional compensation may be awarded after vesting period ends.

Stage 2—Mid-Stage Private (18-36 months to IPO)

As more directors join the team, pay packages tend to homogenize, and many incumbents, by now, are fully vested. At this stage, RSUs begin to outnumber stock options, and awards may be expressed in dollar values instead of company percentages, although there can still be a focus on basis points conversion in some cases. Compensation values range considerably based on the size of the company and the years covered, with packages generally moving towards a front-loaded dollar value intended to cover 3-4 years, ranging from $300k-$700k, but can go up to $1.0M to $2.0M. These higher ranges are often for higher-valuation companies that have a path to IPO and need a highly-experienced director.

Overall, the equity component of a director's compensation now begins to parallel the employee compensation structure, with the same vehicles and grant methodology. As a good rule of thumb, directors' packages should not be considered "more risky" than executive packages, making it likely that weighting of RSUs and options will be the same for each group or lean more towards RSUs for directors.

That said, unique circumstances surrounding a new hire can open up opportunities to negotiate individual packages. This is especially true if the incoming director offers the company valuable skills or perspectives that it urgently needs to add. While still rare, cash compensation becomes slightly more likely at this stage. It may also be possible to adjust vesting schedules.

Stage 3—Preparing to Go Public (<18 months to IPO)

With the IPO approaching, focus often shifts towards recruiting the fully independent board. In anticipation of going public, compensation programs move towards a public company model. At this point, benchmarking of public peers begins to play a larger role in establishing pay practices, and the pay structure will vary based on company size and the aforementioned peer benchmarks.

Cash compensation and short-term RSUs, as a result, grow in prominence. Total compensation for new directors frequently hovers between $250k-$350k annually, and includes a mix of cash and equity. There may still be some initial equity awards issued in order to stake new directors, however, which are typically the same as the annual equity award going forward.

Pre-IPO Compensation Stages

	Stage 1 (>36 Months Pre-IPO)	Stage 2 (18–36 Months Pre-IPO)	Stage 3 (<18 Months Pre-IPO)
Context	• Occurs during B or C-series funding • Often hiring the first outside director	• Occurs during D or E-series funding • Recruiting multiple new directors • Incumbents often fully vested	• Occurs in the last stages of funding • Recruiting final new directors before going public • End goal is a fully independent board going forward
Pay Structure	• RSUs or stock options • Intended to cover multiple years • 3–4 year vesting structure • No cash compensation • Shares granted as a percentage of company	• Typically lean towards RSUs • Intended to cover multiple years • 3–4 year vesting structure • Equity portion of awards frequently matches employee awards • May include cash component • Award expressed as value instead of percentage of company	• Mostly RSUs, mimicking a traditionally public company model • Annual awards typically 1 year vesting • Cash compensation more likely • Awards expressed as value instead of percentage of company
Negotiation Ability	• Highest ability to negotiate total package	• Some ability to negotiate vesting schedule, cash components	• Limited ability to negotiate
Key Considerations	• Highest risk/reward period • Low liquidity • Longest timeline to payout • Typically no refresh awards	• Risk of payout and lack of liquidity still exist but beginning to decline • Typically hiring to fill skill gaps—unique skills may increase leverage	• Lowest risk / highest chance of payout • Highest liquidity • Shortest timeline to payout • May include initial equity awards to stake new directors
Example Median Grant	*20–50bps stake in company with a 4-year vesting period*	*Up front grant valued at $300k-$750k, can be RSU, options, or mix*	*$250k–$350k in annual total compensation, includes mix of cash / equity*

Digging Deeper: Questions and Considerations for Incoming Directors

Directors' compensation packages, particularly in the pre-IPO space, have several unique characteristics that warrant a closer look. If you are thinking about becoming a director for the first time, it is especially important to consider the following:

What happens if the company does not go public?
No matter the company, there is always a risk that IPO plans are scuttled and the company is forced to wind down or sell at a price where common stock is rendered worthless. Without any cash compensation, directors may find themselves working for nothing.

What happens if I leave before the company goes public?
It is important to consider this possibility in initial negotiations, as the terms of your contract will dictate whether or not you will be able to retain your grant. It is important to note that it is highly unlikely you will be able to sell any RSUs on secondary markets, but you may be able to negotiate maintaining your equity to sell in a future IPO, or selling back to company, in the event of an early exit.

Am I willing to lay out cash to exercise my stock options in the event of early departure?
Stock options commonly expire within 90 days of termination, although you may be able to negotiate a longer expiration period.

Am I comfortable with the lack of liquidity?
There is no expectation that directors will be able to participate in pre-IPO liquidity events, as this is generally reserved for employees. The timeline for liquidity can be quite long, and you should be prepared for this possibility.

The Practical Application: Key financial planning considerations for private company directors

Private company directors should engage their advisors early to address key planning considerations when evaluating directorship opportunities. Timely coordination helps efficiently align compensation, tax, and risk strategies with long-term goals.

Maximize long-term value of board compensation via an 83(b) election.

If you receive an actual property interest—like restricted stock or profits interests—as part of your director compensation, you may be eligible to make an 83(b) election. This allows you to pay tax on the value at the time of grant, rather than when it vests, potentially converting future gains that would be taxed at ordinary income rates into long-term capital gains.

The election isn't available for RSUs or standard stock options but may apply if options are early-exercised and converted into restricted stock. For profits interests, which typically have no value at grant, the 83(b) election often results in no immediate tax and locks in capital gains treatment on future appreciation.

Manage risk and understand your exposure

Beyond any company-provided indemnification, Directors and Officers (D&O) insurance is a common consideration for board members. It is important to understand that policy limits may apply to the entire board rather than to individual directors. Directors should ensure they are adequately protected and should confirm the specifics of the D&O coverage with the company and their advisor. Often the most critical part of such coverage is the extent of legal defense reimbursement provided by the policy.

Meet with your advisor early to enact time-sensitive tax and estate planning strategies

It is essential to inform your financial advisor as soon as you join a board, as many planning opportunities are time-sensitive. For instance, the 83(b) election must be filed within 30 days of receiving restricted stock. Other considerations include deferred compensation strategies (which can be tax-efficient and may offer state tax benefits), proper state income taxation sourcing, and the ability to detect business-related expenses. Additionally, directors should ensure that beneficiary designations are up to date and may consider transferring equity to a trust where permitted. Early planning can help maximize the value of board compensation and align it with long-term financial and estate planning goals.

Conclusion: Navigating Compensation with Confidence

Serving on the board of a pre-IPO company can be a rewarding opportunity—both professionally and financially—but it comes with a unique set of risks and considerations. Understanding the nuances of director compensation at each stage of the IPO journey empowers prospective directors to make informed decisions, negotiate effectively, and align their expectations with the company's trajectory.

Whether you're evaluating your first board seat or adding another to your portfolio, the key is preparation. By assessing your leverage, asking the right questions, and engaging trusted advisors early, you can ensure that your compensation package reflects both the value you bring and the risks you assume.

Disclosures

All information and data related to compensation trends and common practices represent the opinion of executive compensation consulting firm Semler Brossy and are based on their experience advising pre-IPO companies on their director compensation plans.

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