Special Purpose Acquisition Companies ("SPACs"): De-SPACing

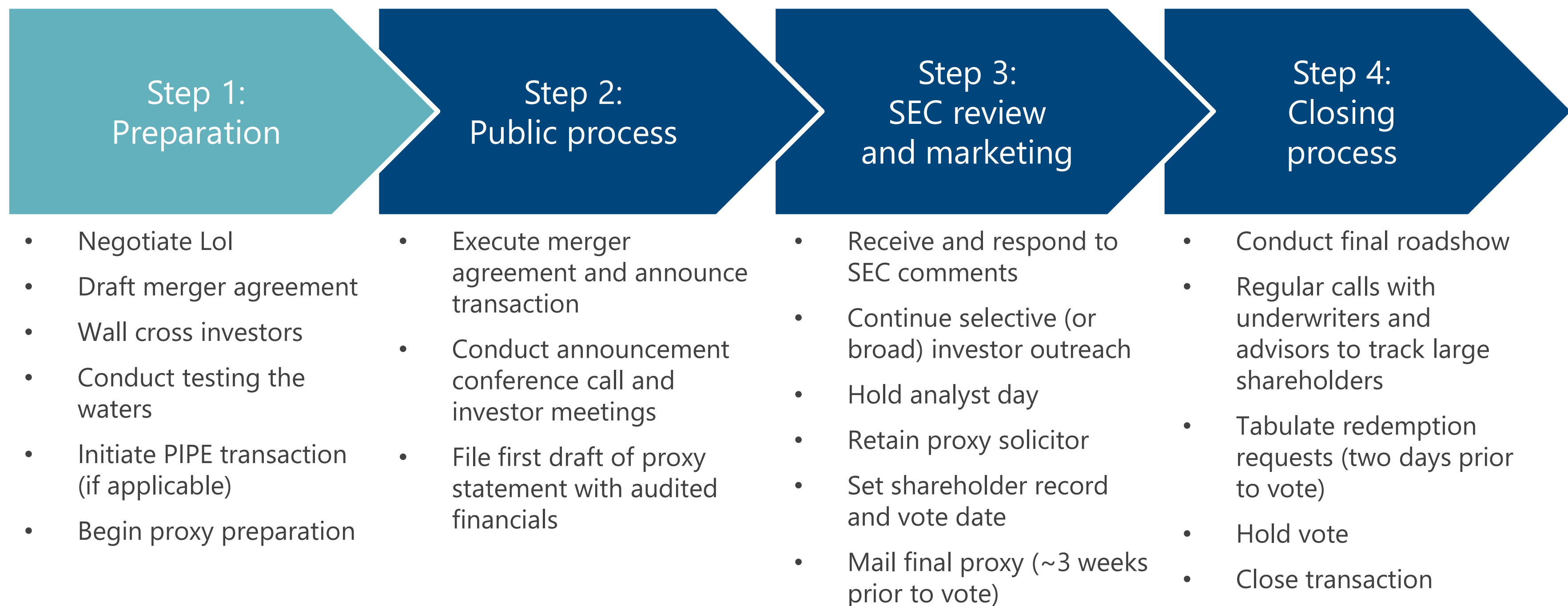
November 2020

De-SPACing

- Process of SPAC acquiring a private company target called “de-SPACing”
- In many respects, similar requirements and process to a public company merger
  - Letter of Intent (“LoI”)
  - Due diligence
  - Merger agreement
- However, there are key differences, such as:
  - Shareholder approval required through proxy statement
  - Redemption opportunity for SPAC shareholders, potentially through tender offer
  - Restrictions post-merger on SPAC holders under securities laws and regulations
  - Greater flexibility (and uncertainty) in purchase consideration
  - Limited recourse if de-SPACing fails

Process overview

- The process from announcement of a definitive agreement (and proxy filing) to close with multiple rounds of investor outreach may take between two and five months



- Timing will depend on the preparation of the proxy statement, the U.S. Securities and Exchange Commission's ("SEC") review of the proxy statement, and the response to those comments
- Often the SPAC sponsor will solicit investor feedback (on a wall crossed basis)
- Best practice is to file proxy statement and release investor presentation as soon as possible after announcing the entry into the definitive agreement
- IPO style roadshow including the target company's management
- Objective is to create enough aggregate demand to absorb any redemptions and to support strong after market performance

Timeline: SPAC merger vs. a traditional IPO

	Weeks 1-4	Weeks 5-7	Weeks 8-10	Weeks 11-12	Weeks 13-16	Weeks 17-19
			SPAC merger completed *(week 10)*			**Traditional IPO completed** *(week 19)*
SPAC Merger	• Finalize diligence and negotiations of identified target • Draft merger proxy document • Announce transaction • **Conduct deal announcement investor presentation** • Finalize merger proxy • File proxy/prospectus with SEC • **Valuation established**	• Obtain initial investor feedback • Monitor trading dynamics • Receive and respond to SEC comments • Develop marketing plan	• Perform detailed investor targeting • **Begin roadshow** • Set record date for shareholder vote • Complete SEC review • **Continue investor roadshow** • Mail definitive proxy and hold shareholder vote • Tabulate votes and redemption requests • Complete SPAC merger			
Traditional IPO	• **Hold org. meeting** • **Prepare due diligence presentations** • **Conduct due diligence** • **Begin S-1 drafting** • Distribute draft legal documents and S-1 • Draft legal documents	• **File S-1 confidentially with financials** • **Begin drafting roadshow, analyst presentation and analyst financial model** • Finalize legal documents for first filing	• Receive first round SEC comments • **Continue drafting roadshow and analyst financial model** • **Invite bookrunners and co-managers** • **Host research analyst due diligence session** • **Bookrunner and co manager due diligence (with projections)** • Refile S-1 confidentially	• Receive second round SEC comments • Refile S-1 confidentially • Analysts draft IPO model • Continue drafting roadshow presentation	• Receive third round SEC comments • Finalize S-1/legal documents • Refile S-1 publicly 15 days prior to launch • Research analyst provide final models • Continue drafting roadshow presentation	• Evaluate market conditions / filing range • Finalize roadshow • Receive SEC clearance and file / print preliminary prospectus • Launch transaction and roadshow • Continue roadshow • **Valuation established** • Price offering • Closing and settlement

SPAC merger process

Identifying target

- SPACs cannot identify specific companies as targets pre-IPO
- Following the SPAC IPO, the SPAC must search for a target and conduct preliminary due diligence
- Not all SPACs are the same
  - Some are focused on a particular geography or industry
  - Others have no such mandate
- NYSE and Nasdaq both have requirements for a SPAC’s target and SPAC
  - Initial business combination must be with a business having an aggregate fair market value of at least 80% of trust account
  - Must complete business combination within 24 to 36 months (or shorter as specified in SPAC registration statement) of IPO registration statement
  - NYSE LCM Section 102.06 and Nasdaq IM Rule 5101-2

- Similar to a public merger, first step is typically letter of intent
- The LoI describes the most important elements of the transaction, including:
  - The structure of transaction
  - Price and consideration (earn out or not),
  - Confidentiality and exclusivity provisions
- The LoI is non-binding, but will include some binding terms, such as:
  - Exclusivity agreements in which the seller agrees not to negotiate a sale with third parties for an agreed period of time
  - Confidentiality agreements
  - Agreements that each party will be responsible for its own transaction expenses

Due diligence

- After LoI, detailed due diligence begins, including but not limited to:
  - Valuation
  - Accounting
  - Legal
  - Tax
- Similar to any acquisition, buyer (*i.e.*, SPAC) usually conducts more due diligence
- Target company should also conduct extensive due diligence on SPAC's sponsor, investors, and potential management structure post-merger.

Deal terms

- Because of shareholder redemptions, amount available to the SPAC uncertain
  - Therefore, transaction agreement usually provides flexibility in terms of consideration
  - Purchase price generally calculated on "cash free/debt free" basis with post-closing true-up, rather than fixed purchase price per share
  - Escrow arrangements and earnouts also common
- Target shareholder consideration usually is a combination of cash and "rollover" equity
  - SPAC sponsors often negotiate for greater "rollover" equity to hedge against cash shortfall due to redemptions
  - Target typically requires "minimum cash" condition and committed acquisition financing
    - Subscription agreements for simultaneous PIPE investment

Deal terms *(cont'd)*

- SPAC transaction agreements generally do not have "fiduciary out" if board of directors changes its recommendation
- Market practice varies with respect to post-closing survival of representations and warranties
  - Some do not survive closing, similar to public company transactions
  - Some deals provide for survival periods for some or all representations and warranties, with recourse to an escrow
  - Representation and warranty insurance becoming more common
- Very limited deal protection
  - Reverse break-up fee from SPAC rare
  - Reimbursement of target's fees and expenses inconsistent

- After definitive merger agreement reached and announced, shareholder vote on the proposed transaction is often required
  - Shareholders also have right to redeem their shares
- SPAC must file proxy statement on Schedule 14A
  - If SPAC intends to register new securities as part of transaction, SPAC must also file a proxy/prospectus on Form S-4
- Proxy statement or proxy/prospectus statement must contain:
  - Financial statements of SPAC, target, and businesses acquired by target
  - Description of post-transaction company and its management, directors, governance structure, and material contracts (including debt financing agreements related to the de-SPACing transaction)
  - Pro forma financial information reflecting proposed acquisition
  - Management's discussion and analysis for the SPAC and for target
  - Selected historical data of SPAC and target, including pro forma financial data
  - Comparative per share information, including pro forma per share data

Shareholder vote and redemption rules *(cont'd)*

- SPAC can also conduct tender offer
  - SPAC will prepare Schedule TO instead of Schedule 14A
  - Schedule TO has similar disclosure requirements as proxy statement
- SEC reviews proxy statements and joint proxy/prospectus
- SEC has a target of issuing comments on such filings within 30 days
- SPAC can expect to receive a few rounds of SEC comments before the proxy statement is mailed to shareholders
- Following SEC review, SPAC mails proxy statement to shareholders for review, meeting, and vote
- Shareholders may vote in favor of the transaction and still redeem their shares
  - LCM Section 102.06 and Nasdaq IM Rule 5101-2(e)

- After deal terms are announced, SPAC sponsors and management will also meet with new investors and analysts
  - Investor presentation usually released in conjunction with announcement
- If new investors purchase stock, SPAC stock will rise above trust value
  - Rising stock will encourage existing shareholders to keep their shares and not redeem
  - Will also support strong after market performance

Renegotiation of deal terms

- Despite flexibility of SPAC transaction agreements, closing conditions may not be met. This may occur due to:
  - High redemption levels
  - Inability to obtain alternative financing within permitted parameters
- Parties have two choices in this situation:
  - Terminate agreement
  - Renegotiate transaction terms
- Because SPAC sponsors have a strong incentive to complete deals, renegotiation more common
- Transaction renegotiation generally takes two forms
  - Deal made more attractive to certain or all public shareholders to decrease redemptions
    - *Example*: Sponsor may agree to forfeit some founder’s shares
  - Target company may agree to waive minimum cash closing condition or accept equity instead of cash, in exchange for target-friendly amendment

- SPACs and target companies often secure additional financing, but this may be at a price per share less than the trust account value per share
- Nasdaq listing standards require minimum number of freely tradeable shares at time of listing

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