Knowledge sharing

What is a SPAC?

September 2019

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Current market for SPACs
Current market for SPACs

The recent resurgence in SPAC IPOs

- SPACs reached a height in 2007, during which 66 SPACs raised a total of $12 billion
- SPAC IPO activity came to an almost complete halt after the great recession, with only one SPAC IPO occurring in 2009, raising $36 million in capital
- In recent years, SPACs have reemerged and are gaining momentum

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of SPACs Completing IPOs</th>
<th>Funds Raised</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019*</td>
<td>39</td>
<td>$9.2B</td>
</tr>
<tr>
<td>2018</td>
<td>46</td>
<td>$10.8B</td>
</tr>
<tr>
<td>2017</td>
<td>34</td>
<td>$10.0B</td>
</tr>
<tr>
<td>2016</td>
<td>13</td>
<td>$3.5B</td>
</tr>
<tr>
<td>2015</td>
<td>20</td>
<td>$3.9B</td>
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</tbody>
</table>

*As of July 31, 2019


SPAC IPO activity in comparison to all IPOs

<table>
<thead>
<tr>
<th>Year</th>
<th>SPAC IPO # of Deals / Gross Proceeds</th>
<th>All IPOs # of Deals / Gross Proceeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>2019*</td>
<td>39 / $9.2B</td>
<td>107 / $42.5B</td>
</tr>
<tr>
<td>2018</td>
<td>46 / $10.8B</td>
<td>191 / $46.9B</td>
</tr>
<tr>
<td>2017</td>
<td>34 / $10.0B</td>
<td>160 / $35.5B</td>
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- In the first three quarters of 2019, SPACs represented 36.8% of the total IPO market by deal count and 21.5% of the total IPO market by dollar amount raised.

*As of July 31, 2019
**Increase in size of SPAC offerings**

**Recent trend towards larger IPO sizes**

- The average size of SPAC IPOs jumped from $144 million in 2013 to $294 million in 2017, a 104% increase

- The SPAC IPO market remains strong in 2019 with 39 completed IPOs raising an average of $234 million per offering

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**In 2018, the three largest SPAC IPOs included:**

- **Churchill Capital** – priced on September 11 and raised $690 million  
  *Sole Underwriter: Citigroup Global Markets Inc.*

- **GS Acquisition** – priced on June 7 and raised $600 million  
  *Sole Underwriter: Goldman Sachs*

- **Far Point Acquisition** – priced June 11 and raised $550 million  
  *Underwriters: Credit Suisse and Bank of America Merrill Lynch*
Current market for SPACs

- Despite their successful marketing, SPACs have had mixed success finding acquisitions
  - Of the 368 SPACs that have completed IPOs since 2003:
SPAC structure
What is a SPAC?

Special purpose acquisition company

- Business entity organized to raise capital in an IPO in anticipation of identifying and acquiring one or more operating companies through a business combination
  - Target company cannot be identified before IPO is completed
  - SPAC doesn’t have commercial operations until first combination is consummated at which time the target becomes publicly traded

- Typically formed by sponsors that believe that their experience, reputations and access to proprietary deal flow will allow them to identify and complete a business combination with one or more companies that will be successful as a public company

- Provides investors with public company transparency, liquidity and rights to approve the business combination
  - Specified deadline for completion of business combination – typically 18-24 months
  - Investors can reject business combination and receive pro rata portion of IPO proceeds that are held in a trust account

- Generally exempt from “Blank-Check Company” Rule 419
**SPAC vs. blank check company**

A SPAC is exempt from regulation as a Blank Check Company under Rule 419 on the basis that its net tangible assets exceed $5 million

— Rule 419 imposes various onerous requirements on Blank Check Companies, including prohibition on trading of its common equity until an acquisition occurs

— While not required, SPAC offerings generally follow the spirit of Rule 419 offerings with a few significant differences
  
  • 90+% of net proceeds deposited in escrow
  • Fair value of first targeted business to represent at least 80% of the amount held in trust
  • Units issued in SPAC offerings begin trading on date of IPO
    • Units are composed of common stock and warrants that are intended to provide investors with compensation for having funds held in escrow
    • Warrants enable investors to invest more capital at a pre-determined price and leverage initial investment
## SPAC vs. blank check company

<table>
<thead>
<tr>
<th></th>
<th>SPAC</th>
<th>Blank Check Company</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Escrow of offering proceeds</strong></td>
<td>At least 90% of proceeds from the offering and private placement are deposited in a trust account</td>
<td>The gross proceeds, less allowable underwriting commissions, expenses and company deductions under Rule 419, are deposited into an escrow account</td>
</tr>
<tr>
<td><strong>Investment of net proceeds</strong></td>
<td>Net offering proceeds are invested only in securities that are direct obligations of, or obligations guaranteed by, the United States, with a maturity of 180 days or less or in money market funds meeting conditions under Rule 2a-7 of the Investment Company Act</td>
<td>Proceeds can only be invested in specified securities, such as a money market fund or in securities that are direct obligations of, or obligations guaranteed by, the United States</td>
</tr>
<tr>
<td><strong>Receipt of interest on escrowed funds</strong></td>
<td>Interest on proceeds from the trust account is paid to investors</td>
<td>Interest on funds in escrow is held for the sole benefit of investors</td>
</tr>
<tr>
<td><strong>Limitation on fair value or net assets of business</strong></td>
<td>Nasdaq rules dictate the initial business combination must be with one or more target businesses that together have a fair market value equal to 80% of the balance in the trust account</td>
<td>The fair value or net assets of a target business must represent at least 80% of the maximum offering proceeds</td>
</tr>
</tbody>
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## SPAC vs. blank check company

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<td><strong>Trading of securities issued</strong></td>
<td>The units may trade before the initial business combination so long as the SPAC files a Form 8-K including updated financial information</td>
<td>No trading of the units or the underlying ordinary shares and warrants is permitted until the completion of a business combination</td>
</tr>
<tr>
<td><strong>Exercise of the warrants</strong></td>
<td>Warrants cannot be exercised until the later of 30 days after the completion of the initial business combination or 12 months from the closing of this offering</td>
<td>Warrants could be exercised prior to the completion of a business combination but securities received and cash paid would be deposited into the escrow account</td>
</tr>
<tr>
<td><strong>Election to remain an investor</strong></td>
<td>A shareholder vote may not be required. If there is a shareholder vote, a SPAC may offer to redeem shares</td>
<td>A prospectus regarding the business combination would go to each investor, who would have the opportunity to decide if he or she elects to remain a shareholder or require the return of his or her investment</td>
</tr>
<tr>
<td><strong>Business combination deadline</strong></td>
<td>An acquisition must be completed within 24 months</td>
<td>An acquisition must be completed within 18 months</td>
</tr>
<tr>
<td><strong>Release of funds</strong></td>
<td>The proceeds will not be released until the earliest of the completion of the initial business combination, the redemption of any shares in connection with a shareholder vote, or the redemption of shares if unable to complete a business combination within 24 months</td>
<td>The proceeds held in escrow are not released until the earlier of the completion of a business combination or the failure to effect a business combination within the allotted time</td>
</tr>
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</table>
How are SPACs structured?

- Founders (i.e., the SPAC management team) invest initial capital to form the SPAC
  - Founders’ shares typically sold for nominal value
  - Designed to ensure founders retain 20%-25% of equity after the IPO and incentivizes management to find and close a business combination

- IPO consists of units, composed of shares and warrants
  - Warrants are typically issued out of the money and are exercisable only upon completion of a business combination

- SPACs are subject to restrictions on operations
  - Deadline for business combination (e.g., 18-24 months)
  - Size requirement for business combination (e.g., 80% of net assets)
  - No compensation to founders prior to combination

- SPACs have Audit Committee and corporate governance structures similar to other operating companies

- Underwriters play a large role in the structuring of a SPAC

- Significant percentage of IPO proceeds, at least 90%, are placed in a trust account until business combination or liquidation
How are SPACs structured?

Founders and management team

- Well-known private equity and hedge fund operators
- Current and former investment company managers
- Assorted politicians and corporate executives
- Notable officers include:
  - Former counterterrorism official Richard Clarke
  - Former Apple executives Steve Wozniak, Gilbert Amelio and Ellen Hancock
  - Former Congressman Thomas McMillen
  - Former undersecretary for federal Department of Homeland Security Asa Hutchinson
  - CEO of Solar Capital Michael Gross
  - Former oil executive Tony Hayward
  - Former Facebook executive Chamath Palihapitiya
How are SPACs structured?

Securities offered

- Units offered in IPO consist of:
  - One share of common stock
  - One to two warrants exercisable for one share of common stock
    - 1/2 and 1/3 of a warrant offered recently (which reduces overhang)
  - 1/2 and 1/3 of a warrant offered recently (which reduces overhang)

- IPO price typically set at $10.00 per unit

- Units typically separate on a voluntary basis into components 52 calendar days after the date that the IPO commences
  - Subject to the issuer filing an 8-K with financial statements

- Warrants not exercisable until consummation of a business combination or liquidation
  - Exercise price varies based upon IPO price ($5.00 to $12.00) depending on the exercise ratio from warrants to common stock, which can range from 3:1 to 1:1
  - Warrants are typically issued *out of the money* (115%-120% of unit offering price)
  - Redeemable for nominal value if SPAC shares trade above set market price
How are SPACs structured?

Trust account

– Many offerings include terms requiring a greater percentage of IPO proceeds (up to 100%) held in trust account
  • Fund additional amounts through private placement by insiders concurrent with IPO
  • Use of deferred underwriting discounts
  • Provides greater protection for investors, coupled with greater risk for insiders/underwriters

– IPO proceeds are invested either in US treasury bills with a maturity of 180 days or less or money market funds

– Some disbursement of interest permitted to pay income taxes and for use as working capital
  • However, some deals limit the amount of interest that can be used as working capital and the circumstances in which interest on IPO proceeds can be disbursed

– Should obtain waivers against trust when entering into agreements to protect against liability
How are SPACs structured?
Optional structural elements

- Additional features either to satisfy market expectations or as a result of agreements involving the founders and underwriters:
  - Lock-up agreements and registration rights agreements
  - Pre-IPO sponsor warrant purchase commitment agreements
    - Purchase of warrants occurs concurrent with IPO closing
  - Redemption rights for public shareholders upon completion of the initial business combination
  - Co-investment rights – sponsor commits to pre-defined open market purchases of shares under a 10b-5(1) plan
  - Right to acquire shares post-business combination
  - Lower up-front underwriting fees (2%-3%), with remainder payable upon successful completion of business combination
  - Shareholder vote features to reduce impact of votes “against”
    - Increased redemption thresholds
    - Ability to vote “for” business combination and still opt to get money back
    - Tender offer for shares of common stock upon completion of business combination
Founder warrant purchase commitments

— Historically, management obligated to buy warrants in the aftermarket after the IPO
  • Served to align management and investor interests
  • Arguably provided increased liquidity for warrants

— The current practice is for founders to acquire warrants directly from the SPAC
  • Purchase occurs concurrently with the closing of the IPO
  • Proceeds are generally placed in a trust account
  • Sponsor’s “at risk” capital is approximately 5% depending on the size of the SPAC

— Sponsor’s shares/warrants usually subject to clawbacks and/or structured lock-up releases
  • Sponsors have potential to own 20%-25% of the company after the business combination is completed
Sample SPAC deal flow

1. Initial capitalization, Founders and Board purchase 10,000,000 shares of common stock for $20,000

2. In IPO, investors purchase 40,000,000 units for $400,000,000, each unit is composed of 1 share and 1 warrant. Warrants are convertible into 1/3 of a share of common stock.

3. Per written agreement, Founders purchase 20,000,000 private placement warrants for $10,000,000.

4. SPAC acquires Target for $400,000,000. Founders now own 20% of Opco Shares, Investors own 80%.

5. Shareholders vote to approve an acquisition for $400,000,000 cash, no shareholders redeem shares.

6. All outstanding warrants are exercised and converted into common shares. Founders now own 25% of Opco Shares, Investors own 75%.
Selection of prospective target operating companies

- Some SPACs have limited their scope of prospective operating companies to focused market segments
- SPACs do not have to limit their scope but can choose to target a company in any field or any market
- Recent market trend is toward specific niche sectors
  - Energy
  - Healthcare
  - Technology
  - Real estate
  - Entertainment/media
  - Water
- Specific investments include:
  - Chinese men’s fashion
  - Mexican fast food
  - Truck accessories
  - Agricultural innovations
  - International fishing fleet
  - Space exploration
Business combination restrictions

– Fair market value of target business must exceed 80% of a SPAC’s trust account assets per listing standards

– Strict deadline for business combination
  • Must consummate a business combination within 18-24 months of IPO
  • Extensions may be granted by a vote of the shareholders (e.g., Jensyn Acquisition Corp. and Easterly Acquisition Corp.)

– Stockholders who vote against the combination have the right to convert their shares into a pro rata interest in the escrowed IPO funds

– If a specified percentage (typically 19.99%-29.99%) exercise such conversion rights, the combination will not be completed and the SPAC will be liquidated
  • Some deals had conversion threshold set at 90%
    • $5 million must remain in trust plus funds for deal expenses
Charter conversion limitations

- Some SPACs had difficulty completing business combinations due to institutional investors gaining control of more than the conversion threshold and voting “no”

- In response, some SPACs include in their governing documents limits on how much an individual public stockholder’s position may be converted into cash held in trust if they vote against the business combination
  - Restricts conversion rights of more than 10%-20% of IPO shares even though can still vote all shares against the transaction

- Restriction should prevent accumulation of large blocks of stock before vote on business combination
  - Limits attempts to use conversion right as a way to force SPAC to purchase activist stockholder’s shares at a significant premium to the public price
  - Limits the ability of a small group of stockholders from blocking a business combination that is favored by most other stockholders
The IPO process
Primary regulatory steps in the IPO process

- Prepare and file Form S-1 registration statement with SEC
- Select and file listing application with a trading market
- Make filing with FINRA regarding underwriting compensation and arrangements
SEC review of the IPO process

- Review and comment on Form S-1
  - Focus on disclosure
  - Not merit-based evaluation of offering
- Form S-1 assigned to one of the Disclosure Operations section of the SEC’s Division of Corporation Finance
- Disclosure Operation is divided into 11 groups, organized by industry type. SPACs, however, may be assigned to any group
- Long-standing Division of Corporation Finance practice to provide comments within 30 days of filing of Form S-1 and within five days of filing subsequent pre-effective amendments
SEC review of the IPO process

A SPAC promoter can facilitate a smoother SEC review

— Avoid taking any steps to search for or locate a target business before and during an IPO
— Avoid any contacts, preliminary or otherwise, with potential target businesses before and during an IPO
— To the extent possible, limit conflict of interest-related relationships and transactions, and provide detailed disclosure to the extent there are any conflicts
Exchange or trading market
Main factors to consider

— Historically, most SPACs had their securities quoted on the OTC-Bulletin Board
  • Securities quoted on the OTC-BB are not “covered securities” under federal securities laws and therefore subject to blue sky regulation
  • Limits investor pool largely to institutional investors because of state blue sky exemptions for offerings to such investors
  • Costs associated with “blue-sky” compliance

— Currently, both Nasdaq and the NYSE permit SPAC listings
  • Listed SPACs are exempt from “blue sky” regulation
  • Listing fees and officer annual affirmation requirements apply
  • Additionally, listed SPACs must comply with listing standards
Exchange or trading market

- In 2008, both Nasdaq and NYSE filed proposed rule changes with the SEC to permit SPAC listings
- Many of the listing requirements are the same
- Since 2011, in order to eventually list on a national exchange as the acquisition company, the SPAC’s shares must previously be listed on the exchange to fit into a carve-out from the definition of “reverse merger”
# Nasdaq vs. NYSE listing standards

<table>
<thead>
<tr>
<th></th>
<th>Nasdaq</th>
<th>NYSE</th>
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<tbody>
<tr>
<td><strong>Issuer Requirements</strong></td>
<td>Securities listed on Nasdaq must have at least 300 round lot shareholders upon listing and at least 50% of such round lot shareholders must each hold unrestricted securities with a market value of at least $2,500. In addition, there must be at least 1,000,000 unrestricted publicly held shares. SPACs must also demonstrate an aggregate market value of $50,000,000, a market value of publicly held shares of $15,000,000 and have a closing price or an IPO price per share of at least $4 at the time of initial listing.</td>
<td>Securities listed on NYSE must have at least 300 round lot shareholders upon listing and 1,100,000 publicly held shares. SPACs must demonstrate an aggregate market value of $100,000,000, a market value of publicly held shares of $80,000,000 and have a closing price or an IPO price per share of at least $4 at the time of initial listing.</td>
</tr>
<tr>
<td><strong>Corporate Governance Requirements</strong></td>
<td>SPACs must generally meet all corporate governance requirements.</td>
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</tr>
<tr>
<td><strong>Deposit/Trust Account</strong></td>
<td>At least 90% of the proceeds raised in the IPO and any concurrent sale by the SPAC of equity securities must be deposited in a trust account, an escrow account or in a separate bank account (collectively, a “deposit account”).</td>
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</tr>
<tr>
<td><strong>Deadline for Completing Business Acquisition</strong></td>
<td>Within 36 months of the effective date of its IPO registration statement, or such shorter period that the company specifies in its registration statement, the SPAC must complete one or more business combinations having an aggregate fair market value of at least 80% of the value of the deposit account (excluding any deferred underwriters fees and taxes payable on the income earned on the deposit account) at the time of the agreement to enter into the initial combination.</td>
<td>The SPAC will be liquidated if no business combination has been consummated within a specified time period not to exceed three years. The SEC will promptly commence delisting procedures with respect to any SPAC that fails to consummate its business combination within (i) the time period specified by its constitutive documents or by contract or (ii) three years, whichever is shorter.</td>
</tr>
<tr>
<td><strong>Board Approval</strong></td>
<td>Each business combination must be approved by a majority of the company's independent directors.</td>
<td></td>
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<tr>
<td><strong>Shareholder Approval</strong></td>
<td>Each business combination must be approved by a majority of votes cast at the shareholder meeting at which the business combination is being considered.</td>
<td></td>
</tr>
<tr>
<td><strong>Redemption Rights</strong></td>
<td>If a shareholder vote on a business combination is held, each public shareholder voting against a business combination must have the right to convert their shares of common stock into a pro rata share of the aggregate amount then in the deposit account (net of taxes payable and amounts distributed to management for working capital purposes) if the business combination is approved and consummated.</td>
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FINRA’s role in the IPO process

– FINRA, a self-governing body of which the underwriters are member firms, will review the proposed offering arrangements to determine whether the underwriters’ compensation for the offering is “fair and equitable” to the SPAC

– Prior to commencing an IPO, the underwriters must receive a “no-objection letter” from FINRA

– Underwriting compensation is broadly defined and may include
  • “Purchase options” issued to underwriters
  • Fees received both for IPO and for subsequent advisory work (e.g., for aftermarket warrant solicitations and evaluation of potential acquisition candidates)

– FINRA set forth guidance on SPACs in 2008
Regulatory obligations of SPACs after an IPO

— SPACs must file Form 10-Ks, Form 10-Qs, Form 8-Ks and proxy statements with the SEC
  • Executive officers and directors must file Section 16 personal securities holdings reports with the SEC

— SPACs must comply with the Sarbanes-Oxley Act of 2002, including Section 302 and 906 certifications, and the corporate governance listing standards of Nasdaq or NYSE, including director independence

— SPACs may take advantage of Emerging Growth Company Status of the 2012 JOBS Act

— SPACs must comply with the Dodd-Frank Act of 2012 to the extent applicable
Operating concerns of SPACs after an IPO

— Investing proceeds held in the trust account to avoid being deemed an “investment company” under the 1940 Act
— Finding a suitable acquisition candidate within the required time frame
— Ensuring that the proceeds held outside of the trust account or the interest generated thereon (depending on how the IPO was structured) are sufficient to pay operating expenses, including those expenses necessary to consummate a business combination
Important steps in consummating a business combination transaction

- Search for a target business
- Conduct due diligence
- Negotiations/break-up fees
- Enter into an agreement for a business combination
- Proxy/registration statement
  • Subject to full review by the SEC
- If multiple business combinations, SPAC must coordinate closings
Eversheds Sutherland capital markets & securities

Contact us

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Our team includes attorneys who previously served on the staff of the US Securities and Exchange Commission, and we routinely interact with SEC staff members in connection with the filing of registration statements and other securities filings.

Our team is highly experienced in successfully completing securities offerings of all types. Since 2006, we have been involved in raising more than $50 billion in capital in hundreds of public and private capital transactions. We have the breadth, depth and experience to complete complex capital formation transactions efficiently. Our securities team is highly experienced in successfully completing offerings of all types including:

- Private placements of debt and equity
- Initial public offerings and follow-on equity offerings
- Secured and unsecured public debt
- Convertible debt
- Stock exchanges, tender offers and stock repurchase programs
- Sales of stock by insiders and other selling stockholders
- Transferable and non-transferable rights offerings

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