

Key Deliverables For SPAC Parties Amid Growth Trend

By Josh DuClos (February 12, 2021)

Special purpose acquisition companies, or SPACs, leapt to fame in 2020 with 248 SPAC initial public offerings raising over \$83 billion, and they continue to gain momentum as we head into 2021.

As of Feb. 12, 2021, in the first 43 days of 2021, according to Spacinsider.com, there have already been 144 SPAC IPOs raising nearly \$44.3 billion, vastly eclipsing all of 2019 and positioning 2021 to significantly outpace 2020 for SPAC IPO activity.



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The stage is therefore set for an explosion of de-SPAC business combinations. As operating companies, sponsors and their SPACs begin discussions about a possible business combination, there are some key timing and process points for both parties to consider, and critical courses to chart, to ensure smooth sailing ahead. As with any deal, timing is everything.

Avoiding Accounting Pitfalls

One of the most common mistakes many SPAC transaction participants make is not thinking early on in the process about the financial statements and audits required by the U.S. Securities and Exchange Commission as part of the registration or proxy statement filed in connection with a de-SPAC transaction, and the impact of producing those financials on the overall timing of a transaction.

Given the long lead times and other milestone events that need to be taken into account, all of which can have an impact on what is required and when it can be produced, these issues should be confronted and mapped out under various timing and structuring scenarios at the beginning of SPAC negotiations, rather than as a technical afterthought.

There are many legal and accounting questions and considerations that go into the analysis of both what financials are required as well as how long it will really take to produce them. These include:

- Which entity is the accounting acquirer based on proposed transaction structure;
- Whether the resulting de-SPACed company would be an emerging growth company or smaller reporting company under SEC rules, and whether the SPAC has already filed a Form 10-K prior to the de-SPAC;
- To what extent public company or Public Company Accounting Oversight Board audits will be required;
- What the target company's private company audits look like, what is its general audit cycle timing; and
- Whether its existing auditors meet public company independence standards.

Finally, it is important to know whether the target company has conducted or will conduct acquisitions itself in the near term that could rise to the relevant significance thresholds under Rule 3-05 of Regulation S-X, which could require certain additional audited financials and pro forma presentation for the applicable target-acquired companies as well.

Additionally, as there are increasingly more SPACs in a crowded market, they may begin taking more time to find the right targets. The potential of complicating milestones in the life of the SPAC itself may come into play, such as how many months have passed since the SPAC's IPO — and whether the target company can take advantage of an initial confidential filing with the SEC as a result — the SPAC's first 10-K filing date, as well as its expiration date and any associated extension requirements.

With these requirements in mind, SPAC participants need to remain keenly aware of the calendar with respect to general market and financing windows, including periodic reporting staleness dates, outside drop-dead dates on the transaction and similar timing of private investment in public equity commitments and other third-party investors with respect to closing and post-closing registration of securities.

Early and Frequent Outreach With Key Company Stakeholders

As more companies find themselves entertaining, and potentially pursuing and negotiating, SPAC business combinations, a larger and more diverse pool of potential stakeholders — management, board members, shareholders, employees, customers and vendors — are concurrently experiencing a baptism by fire when it comes to understanding SPAC transactions, their structure, economics and impacts on the company and themselves.

A SPAC suddenly becomes a lot more tangible and confounding when it moves from a news feed into a shareholder support agreement that has landed in an investor's inbox.

While these groups may have a working familiarity with a traditional M&A or IPO event, chances are that most of these constituents are still on a steep learning curve when it comes to SPAC business combinations. Therefore, companies must consider and plan for early, frequent and strategic outreach to key constituents.

SPAC business combinations are complex hybrids of an M&A, IPO and financing transaction. Depending on exactly how they are structured and financed, they can have dramatically different impacts — legally and practically — on multiple types of third parties and downstream contractual analyses.

SPAC transaction participants, and target companies in particular, should carefully consider the impacts their potential transactions may have on contractual change of control analyses, shareholder approval rights and mechanics, management and employee equity and other compensation arrangements, the order and magnitude of the distribution of proceeds to equity holders, debt repayment or rollover terms, and existing investor rights agreements and arrangements.

Parties should not, for example, want to find themselves in the position of having a fully negotiated and papered deal ready to launch, only to find that a key shareholder with an effective blocking right on the deal as structured is not amendable to its terms or has demands that could delay or unwind the deal.

While parties will have to carefully consider the right time and manner to bring third parties under the tent, given confidentiality concerns, the failure to properly understand how a

transaction could impact key third parties could significantly delay or impede a transaction as otherwise negotiated between a target and a SPAC in a vacuum.

Now more than ever, with the influx of new SPACs and a widening range of target companies, understanding the key deliverables and their related timing, and clearly communicating with all stakeholders, are critical to the completion of SPAC combinations.

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