



SPACs: A New Frontier for Shareholder Activism

As SPACs spawn a new breed of newly public companies, activists are taking notice.

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SPACs Attract Activism

At the same time, the level of shareholder activism against public companies in general remains elevated relative to historical levels. In 2020, more than 400 activist campaigns were launched against public companies traded in a U.S. stock exchange.

Most of these campaigns were so-called “long activism” (agitating for change seeking to drive the stock up) and a minority were “short activism” (publicly criticizing the company or valuation in an attempt to drive the stock down). This is a continuation of a trend of increased activism that has grown throughout the boom in the markets since the financial crisis.

Due to increased competition within the asset class, and a decrease in the number of public companies in the United States during this time period, activists have been forced to look for targets beyond their traditional stomping grounds.

For example, until the past few years certain regulated industries such as insurance and utilities had largely been ignored by activists. Activism outside North America was also sporadic. As a result, the level of de-SPAC activity is effectively chum in the water for many hungry activists.

Nathan Anderson, Founder of Hindenberg Research, predicts, “[SPACs] taken public in 2020-2021 will be a key source of short ideas for the next decade.”

SPACtivism Before the De-SPAC

The life cycle of a SPAC is well established. After a SPAC’s IPO, it will spend 18 to 24 months on a search for a private company (standalone or, in some cases, a spin-off subsidiary of a public company) to acquire.

After selecting a target and agreeing to acquisition terms, the resulting transaction will require the approval of the shareholders of both the acquired company and the SPAC. Assuming shareholder approval is received, this de-SPAC transaction takes effect and the previously private company begins its life as a listed public company.

Activism is present at all stages of the SPAC life cycle, but the risk and nature of activism varies depending on the stage. The potential for activism increases immediately after the SPAC’s IPO.

Before the time a target is found, an activist

may attempt to influence the choice of the target. It is also possible that an activist may at the same time have a stake in a potential target company that they wish to be targeted by the SPAC.

The risk of this activism increases as the SPAC approaches its expiration, which has a punitive impact on the sponsor. As a result, the SPAC sponsor is likely to become more desperate and perhaps less discerning in evaluating acquisitions.

Activism risk continues after a target is selected during the de-SPAC process. Any time there is a shareholder vote on a substantial economic transaction, there is the potential for an investor to agitate against the deal.

In the late 2000s, there was a wave of activism against SPACs prior to a de-SPAC where activists would purchase shares of a SPAC at a discount with the intent of voting down any proposed merger and redeeming their shares for par value. While current SPAC structures have been modified to deter this specific type of activism, the risk of activism prior to a de-SPAC remains.

After the consummation of the de-SPAC, the risk of activism transfers to the newly formed public company.

SPACtivism After the De-SPAC

After the de-SPAC, the newly public company shares many characteristics with a company that recently completed a “regular” IPO. At its core, a de-SPAC is an alternative to a traditional IPO (and, increasingly, direct listings), in which a private company can transition into a public company. Generally, recent IPOs generally experience a “honeymoon” period that insulates them to some degree from both short activism and long activism.

On the short side, attacks immediately after an IPO are relatively uncommon. From a technical perspective the float of available shares of recent IPOs is often small and there are lockups in place for many insiders and pre-IPO investors to prevent them from selling shares during the first few months.

Less tangibly, there is also often a level of excitement in the wake of the IPO. However, as the lockups expire, insiders become allowed to (and do) sell down, and the float expands, the

Increased Activism Risk for Established Public Companies

The presence of so many SPAC vehicles may even have an impact on long activism at more tenured companies.

Activists often demand that a company pursue a spin-off or carve-out transaction. The availability of several hundred potential vehicles to facilitate such a transaction may result in more activists making this demand over the next two years.

This is particularly true as SPACs approach their expiration, and there is a perception that the SPAC sponsors are more desperate to strike a deal. In addition, several well-known shareholder activists have formed SPACs of their own.

It remains to be seen whether and how any of these SPACs may be used to facilitate the goals of the activist, such as in support of a separate activist campaign or perhaps with the goal of using the resulting de-SPAC as a permanent source of capital for future campaigns.



technical limitations on short-selling decrease, and the company becomes susceptible to short attacks.

On the long side, concentrated shareholder ownership through insiders and other pre-IPO investors, who also often maintain board representation, provides substantial protection against activism in the immediate wake of an IPO.

In some cases, with majority control, there is absolute protection against the threat of a proxy contest to change board composition, which is the ultimate weapon of the long activist. In addition, public institutional investors in an IPO have only recently and consciously chosen to purchase the stock because they support the company’s board, management and strategy.

As a result, they are likely to give the company some time and breathing room to execute its strategy. Furthermore, from a tactical perspective, new IPOs have no public track record and stock price history for an activist to criticize.

All these factors reduce the risk of long activism shortly after an IPO. In fact, two years after an IPO the risk of long activism is only two-thirds that

of a tenured public company, and it takes nearly five years of public trading to achieve equivalence.

In turn, many newly de-SPACed companies also expect to enjoy a honeymoon period similar to their traditional IPO peers. Given the similarity in purpose and result between an IPO and a SPAC merger, this is not surprising. Perhaps the greatest protection for both types of companies against a long activist is the significant insider and pre-IPO ownership in the immediate aftermath of going public, which often tends to be paired with board membership.

However, the pace at which immunity from activism fades is much faster for de-SPACed companies. This is due in part to certain aspects of the de-SPAC process, and in part to the nature of many of the companies that are increasingly going public through the de-SPAC process.

A SPAC conducts M&A due diligence on the private company it is looking to acquire, and – if there is a concurrent PIPE – the banks running that process and the institutional PIPE investors participating in it will add a second layer of vetting and validation to the transaction.

However, the de-SPAC process often still does not involve the same level of scrutiny and preparation by an underwriter that is present in an IPO (where an underwriting bank takes on statutory liability under the Securities Act of 1933), nor the same cache of credibility lent by using the name of that underwriter.

It is possible, therefore, that some companies that go public through a de-SPAC might not have survived the traditional vetting present in a traditional IPO. In addition, SEC regulations relating to a de-SPAC -- unlike those for an IPO -- provide a safe harbor for forward-looking statements, which permits financial projections to be used in marketing the deal. This is seen by many early-stage, high-growth companies as a major advantage to the de-SPAC process over the traditional IPO process.

As a result of these differences, certain companies may find themselves able to go public through a de-SPAC at a less mature stage, with a shorter track record and less public company readiness, and after marketing using forward-looking financial projections that look as many as five or more years into the future.

Furthermore, given the large number of SPACs that need to find partners for a de-SPAC in the next 18 to 24 months, there will be fierce competition to find quality private companies that are at the right stage in their evolution to become public. As a result, it is possible that certain SPACs may seek to partner with candidates that are less attractive than they otherwise would have, and which potentially have more weaknesses for activists to attack.

Finally, as a result of this increased activism risk, there is an additional risk of a sort of downward spiral, or self-fulfilling prophesy: if many activists believe there is a higher likelihood of finding an attractive activism target within this universe, then relatively more activists will look toward de-SPACed companies for potential campaigns, resulting in more activism overall and casting a further pall over those companies that access the public markets via this route.

How to Prepare for SPACtivism

As with many things, preparation for potential activism is key. An appropriate defense starts at the formation of the SPAC and continues into the de-SPAC transaction, and finally, with the resulting public operating company.

SPAC Formation and Target Identification

- **Assure Proper Board Composition for the De-SPAC Evaluation:** The SPAC board of directors should have a strong majority of directors who are truly independent of the sponsor. If it is necessary for several directors to have ties to the sponsor, consider using a special committee of independent directors to make recommendations regarding any de-SPAC. These actions protect against not only activism, but also the wave of litigation and SEC scrutiny that is beginning to crest and is typically focused on conflicts of interest between the sponsor and public SPAC shareholders.
- **Perform Extensive Due Diligence on Potential Targets:** SPACs have historically varied widely in the extent of diligence they perform on their potential target companies. It is imperative, however, for a SPAC to approach the de-SPAC as a full-scale acquisition and, as such, perform the same degree of diligence as a strategic or private equity buyer. This diligence will lead to the better choice of targets, afford the ability to correct any issues identified in the process, and give the SPAC the information it needs to properly help the target company prepare to be a public company.

De-SPAC Merger

- **Assure Proper Board Composition and Management Team Preparedness:** Operating in the public sphere is drastically different than operating as a private company. Everything from day-to-day operations to operational planning, budgeting and forecasting is different when you have thousands of owners (ranging from hedge funds and large institutional investors to retail traders) rather than a handful

Not long after the SPAC merger, a company will be held to increasingly higher standards on board and governance practices, eventually in line with more tenured public companies.



of venture capital or private equity firms. Public companies are subject to SEC reporting requirements and the scrutiny of analysts, investors and plaintiffs’ attorneys. The c-suite and the board room should therefore be composed of a diverse and qualified array of experts with public company experience while also maintaining the key talent and leadership required to execute on the strategy.

- **Include Achievable Forecasts:** Understand that optimistic projections provided in conjunction with the merger may be used against a newly public company by activists if they are not achieved. More modest projections may put some pressure on immediate valuation, but will position the de-SPACed company better to meet projections going forward, rather than missing out of the gate. In addition, consider whether the benefit of longer-term forecasts (which are likely to be discounted by potential investors) are worth the potential future consequences of not achieving these forecasts.
- **Adopt Governance That Protects Against Activism:** Consider protective structures such as classified boards and prohibitions on shareholders calling special meetings or acting by written consent. In addition, any standard form charters and bylaws used by newly minted public companies do not typically include more nuanced protections against shareholder

activism. Ensure that these documents have been reviewed by experienced activism counsel.

Post De-SPAC

- **Break-the-Glass Plan:** In the event of a public attack, it is crucial for the company to be prepared to respond in the same news cycle, if necessary. It should include draft “shelf” response press releases as well as a process flow for real-time decision-making and coordination with external advisors. There is no such thing as too early, and this should ideally be developed as part of the public-company readiness efforts during the de-SPAC process.
- **Board and Management Education/Tabletop Exercise:** Educate the board of directors and broader management team on the activism environment and current risk level. Hold mock sessions on a potential activist attack with senior management and/or the board to educate them on how these campaigns unfold.
- **Look for Early Warnings Signs:** Keep an eye out for unusual activity in the shareholder base – it is not uncommon for long activists to acquire toe-hold positions before approaching their targets. In addition, both long and short activists tend to reach out to former employees in an attempt to gather information. Be prepared and coach your teams ahead of time on reporting these communications up the chain and have a boilerplate response plan in advance.
- **Regularly Review Governance Practices:** Not long after the SPAC merger, a company will be held to increasingly higher standards on board and governance practices, eventually in line with more tenured public companies. In addition, consider updating governing documents to update protections against quickly evolving activist tactics. [IR](#)

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