SPACs: Current Market Trends

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Today's Topics

Overview of SPACs

IPO and PIPE Market Trends

The SEC Staff Comments and Disclosures

De-SPAC Trends

Litigation Trends

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Overview of SPACs

SPAC Overview

- Newly formed corporation with no operations
- Raise capital in an IPO that will be used to complete an acquisition of a private company
- Target must **not** be identified at the time of the IPO
- IPO is sold based on the reputation of the sponsor
  - Leverage reputation and network of the sponsor/management team
  - Knowledge within an industry or geographic location
  - Proprietary deal flow and ability to identify attractive acquisition candidates
- SPAC has no operations prior to business combination, at which point target becomes a public company

SPAC Capital Raise

- SPAC conducts an IPO to raise capital, primarily from institutional investors
- IPO raise is typically about 1/5 to 1/4 of expected enterprise value of target to minimize effect of dilution resulting from founder shares and warrants
- The cash raised in the IPO is placed in a trust account and not released until the SPAC completes a business combination or upon a specified outside date (typically 12 to 24 months after the IPO closing) if the SPAC fails to complete a business combination by such date
- In a concurrent private placement, sponsors purchase warrants (or sometimes units) at fair market value with proceeds used to pay IPO expenses plus a specified amount to be held outside the trust account for future expenses; this is the "at-risk capital"
  - The amount of at-risk capital varies as a percentage of SPAC IPO size, with the percentage varying inversely with SPAC size. For a $200 million SPAC, at-risk capital would be approximately 3% of IPO size.
- In some SPACs, the trust account is "overfunded," i.e., an amount greater than 100% of the gross IPO proceeds (i.e., more than $10 per unit) is placed into the trust account to make the SPAC more attractive to IPO investors.

SPAC Units

- Units generally consist of one share of common stock & one full warrant or a fraction of one warrant
  - Warrant coverage depends on size, prominence/track record of sponsors & market conditions
- Warrants provide additional return to the SPAC's IPO investors
- Coverages in recent IPOs have generally ranged from one-half to one-fifth of a warrant; in the past several months, a handful of SPACs in the biotech/life science sector have not included any warrants
- Occasionally, in order to induce investors to purchase securities in the IPO, other securities are included in the units, such as rights that automatically convert into a portion of a share of common stock at the time of the business combination.

SPAC Stockholder Redemption Rights

- SPAC investors can elect to receive their pro rata portion of the trust account (including interest) back in connection with a proposed business combination through redemption of their common stock (or in connection with vote on extension of SPAC)
  - Warrants trade separately from the common stock and a stockholder can retain its warrants even if it elects to redeem
- Investor can elect to redeem regardless of whether it votes for or against the business combination
- Public stockholders can also sell their securities in the open market before or after the initial business combination
- Redemption risk can be mitigated through forward purchase agreements, back-stops or PIPEs and through contractual agreements by public stockholders not to redeem their stock

Structural Alternatives to Enhance Capital Certainty

	ANCHOR COMMITMENT IN THE IPO	CONCURRENT PRIVATE PLACEMENT AT IPO	FORWARD PURCHASE AGREEMENT
Description	Select investor/s indicate interest to acquire units in the SPAC IPO ahead of public launch, on the same terms as all other investors	Select investor/s subscribe for $[X]MM of common stock (or units) in a separate private placement alongside the IPO	Commitment to subscribe for $[X]MM of securities at time of business combination
Certainty of Capital	●●○○	●●●●	●●●●
Market Signaling Benefit	●●○○	●●●●	●●●○
Speed to Market	●●●●	●●○○	●●○○

Warrant Terms

- Warrants are always struck "out of the money," typically at $11.50
- In some cases, the warrant exercise price is adjusted downward if the SPAC raises capital by issuing common stock or equity-linked securities below a specified price, e.g., $9.20 per share, and certain other conditions are met (referred to as the "Crescent term" after the first offering in which it appeared)
- Not exercisable until the later of 30 days post-business combination and one-year post-IPO, and expire 5 years post-IPO
- The common stock and warrants included in SPAC units can be separated shortly after the IPO, and the warrants and common stock will each trade separately in addition to the unseparated units
- The warrants have no value if a business combination is not completed

Warrant Redemption

- Warrants are redeemable by the SPAC post-business combination for $0.01 per warrant if the trading price reaches a specified threshold, typically $18
- In many cases, the warrants are redeemable for $0.10 per warrant upon 30 days' notice if the common stock is trading at or above $10, provided that warrant holder can exercise the warrant on a cashless basis and receive a fixed number of shares based upon the trading price and time to expiration at the time of redemption
- Some SPACs have sought warrant holder approval to amend the terms of the warrants so that the warrants are mandatorily exchanged at the closing of the business combination for cash and/or stock
- SPACs may also decide to tender for the warrants post-closing to reduce "overhang"

Founder Shares

- In connection with the formation of the SPAC, the SPAC's sponsor acquires founder shares for nominal consideration (generally $25,000)
- Typically results in the SPAC's sponsor owning 20% of outstanding common stock post-IPO
- In connection with negotiation of business combination, SPAC sponsor may agree with the seller to forfeit a portion of the founder shares or subject a portion to performance vesting
- Generally subject to lock-up for 1 year following business combination (with potential earlier release beginning after 180 days if stock trades above a threshold price)
- Often issued as a separate class of stock (class B or class F shares) and convert into class A common stock on a 1:1 basis upon completion of the business combination
  - Conversion ratio subject to anti-dilution adjustments in the event common stock or other equity-linked securities are issued, e.g., in connection with PIPE financing (but no adjustment for shares issued to the seller in the business combination)
  - Anti-dilution adjustments can be waived by the sponsor
  - Usually, only founder shares vote on the appointment of directors prior to business combination

Illustrative SPAC IPO Terms Summary

Terms Under Typical SPAC Structure	
Price per Unit (share of common stock)	$10 per unit (will begin trading at market price immediately following pricing of IPO); unit consisting of one share and a warrant or fraction of a warrant
SPAC Duration	12–24 months; often with the option to extend by depositing additional funds in the trust
Warrant Exercise Period; strike price	5 years with $11.50 per share exercise price
Warrant Redemption	If stock trades above specified price per share for 20 business days in a 30-day period (generally $18); many deals also allow forced cashless exercise if trading above $10 per share for reference period with number of shares issued upon exercise based on date and trading price of common stock
Sponsor Promote/Terms	Generally 20 percent of post-IPO shares (taking into account exercise of over-allotment option); can be structured so that founder shares are “class B common stock” that provides for antidilution to gross up founder shares to take into account PIPE financing
Warrant Coverage; Rights	Generally ranges from 1/5 of warrant to one warrant; occasionally deals issued with a “right” to purchase common stock as part of the unit (e.g., right to 1/10th of share)
Trust Account Funding	Market historically had 100% of proceeds deposited in Trust, but recently the Trust Account has been over-funded in many deals
Withdrawal of Interest from Trust Account	Not all SPACs permit sponsor to withdraw interest on the Trust Account; some SPACs permit sponsor to withdraw interest to pay taxes, and recently, some permit withdrawal to pay regulatory expenses
Stock Exchange Listing	NYSE/Nasdaq
“Crescent” Term	If included, PIPE priced below threshold, then warrant strike price resets so that 115% out-of-the-money; threshold generally $9.20 or $9.50 but can be higher or lower

IPO Process

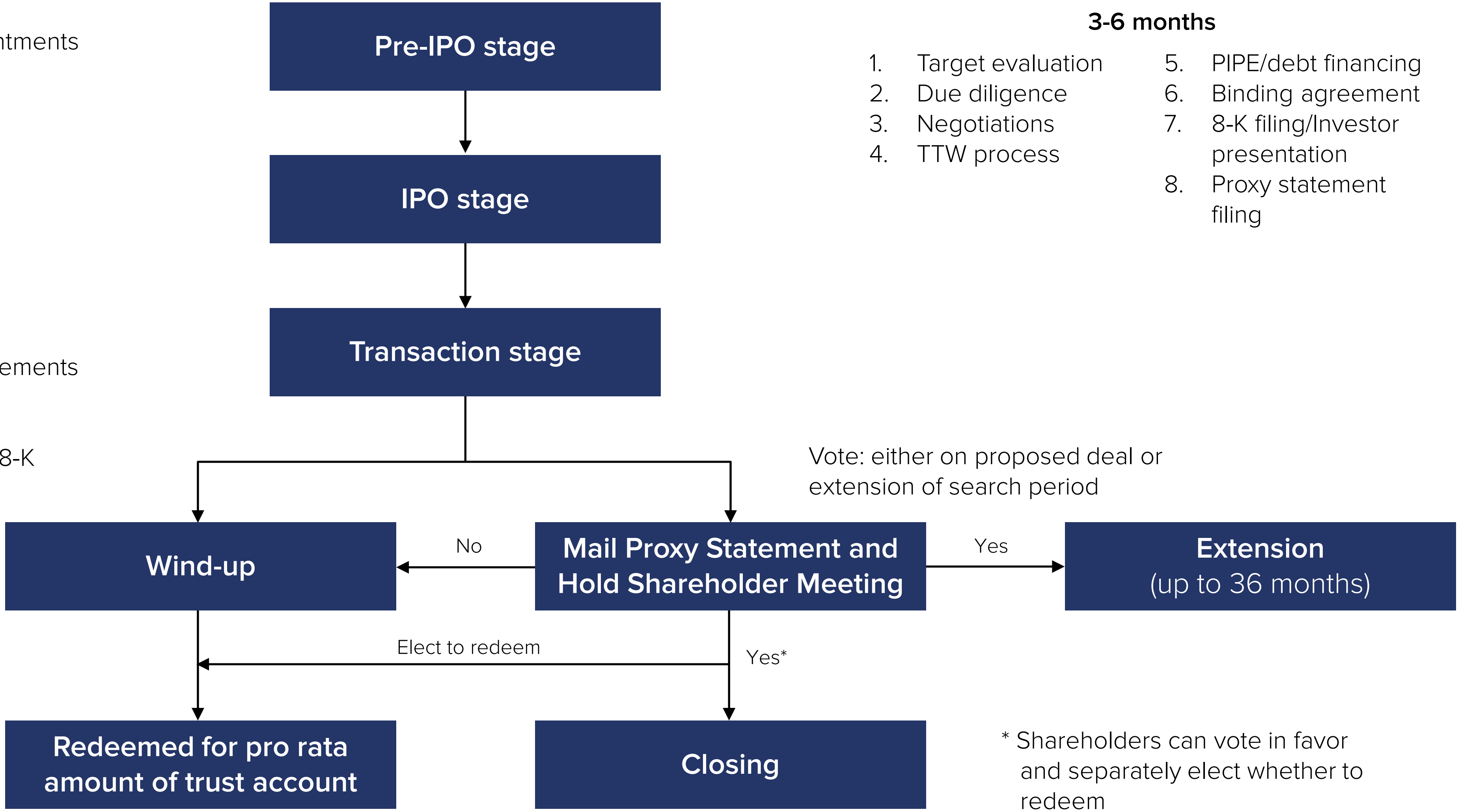
- SPACs conduct their IPOs by filing a Registration Statement on Form S-1 with the SEC, just like other companies conducting IPOs
  - SPACs are “emerging growth companies” under Section 2(a)(19) of Securities Act
  - Can make confidential submissions of draft registration statements under Section 6(e) of Securities Act
    - Must file S-1 publicly at least 15 days before roadshow
- At the time of its IPO, SPAC cannot have selected a business combination target; otherwise, it would have to provide disclosure regarding that target
- A SPAC is an “ineligible issuer”
  - Not entitled to use a free writing prospectus
  - Cannot file automatically effective registration statements

Process Timeline for SPAC Transactions

Initial Actions
- Team & Board appointments
- Investment strategy
- Retain advisors
- Pre-IPO investment

2-3 months
- Background checks
- S-1 filing
- Roadshow
- Initial Public Offering

12-36 months
- Prepare financial statements
- Tax filings
- Board meetings
- SEC filings – 10-Q/K, 8-K



3-6 months

1. Target evaluation
2. Due diligence
3. Negotiations
4. TTW process
5. PIPE/debt financing
6. Binding agreement
7. 8-K filing/Investor presentation
8. Proxy statement filing

Vote: either on proposed deal or extension of search period

* Shareholders can vote in favor and separately elect whether to redeem

IPO and PIPE Market and Terms

CLE Code

- CLE Code: 50421
- A CLE Code Form will be distributed in our post-event email
- Please return completed forms to CLE Lewis Marin at lmarin@winston.com to receive credit

IPO: Trending Market Terms and Actions

- Anchor Investors:
  - Usually 4.9% or 9.9%
  - Will ask for Founder Shares in the ~2-4% range
- Overfunding the Trust Account
  - Typically funded at $10.10 or $10.20
  - Creates interest at the IPO stage by creating more yield
- Shorter Terms for SPACs
  - Can be 12 or 15 months instead of 18 or 24 Months
  - Parties can pay to extend the duration of the SPAC by depositing additional funds int the Trust Account
- Underwriters Compensation
  - Varying in amount; some portion in shares or units

PIPE Trends

- Process Overview
  - Step 1
    - Engagement Letter and Wall Cross Procedures are sent to the SPAC
    - Wall Cross Procedures are sent to other Placement Agents and target
  - Step 2
    - Placement Agents bring investors "over the wall" and investors conduct due diligence
  - Step 3
    - PIPE marketing presentations / roadshows
  - Step 4
    - Sign subscription agreements with investors
  - Step 5
    - Rollout the transaction to market

PIPE Trends (cont.)

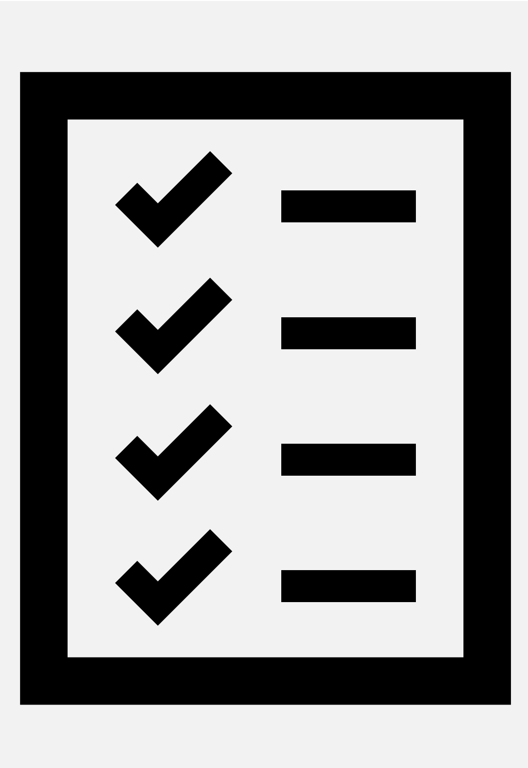
- Alternative Financing Trends
  - Trends
    - SPACs are beginning to offer convertible debt, preferred shares, rights, warrants/lockups, Sponsor backstops, and creative financing structures to early investors
  - Pros
    - Fluid and faster
    - Offers alternative terms that can be tailored to each SPAC and target
    - Creates greater investor interest and can make an investment “more competitive” in a crowded field.
  - Cons
    - Can increase or create debt for the post-closing entity
    - Can decrease certainty regarding redemptions depending on the alternative financing method used

The SEC's Recent Comments & Changes to Disclosure Requirements

Recent SEC Comments

- Enhanced disclosure requirements revolving around China:
  - Variable interest Entities (“VIEs”), PRC regulations; Risks related to doing business in China; Policy risk of foreign investment in China.
- Increased review of F-4/S-4
  - The head of the SEC has even taken to reviewing filings

Question Target Should Prepare to Answer



- Was any consideration provided in exchange for Shareholders to waive redemption rights?
- Include additional Q&A quantifying dilution that shareholders may experience
- What are potential impacts of redemptions on per share value at different redemption values

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Current de-SPAC Transactions: Where the Market is Headed

M&A Timeline ("De-SPACing")

Pre-Public Announcement

T minus 45

- SPAC and target agree on terms through letter of intent

T minus 30

SPAC and target "market" transaction to existing and potential investors (i.e., PIPE investors)

SPAC "wall crosses" investors; confidentiality agreements of specified duration after which SPAC must "cleanse" investors of any MNPI (generally cleanse deal announced or negotiations have ceased)

Definitive Documents/Announcement

Post-Public Announcement

T

Sign agreement; file Form 8-K with investor presentation

T plus 0 to 14

- File proxy statement (or registration statement, depending on structure)

T plus 30 to 44

- Receive SEC comments 30 days after filing

T plus 60 to 75

- Respond to SEC comments and finalize and mail proxy

T plus 80 to 95

- Stockholder vote is held; time from mailing to vote is typically about 15–20 days

  Stockholders can elect redemption up to two days before meeting

2–5 days after stockholder approval

Close transaction

Process Timeline for SPAC Business Combination

Transaction (3-6 months)

- Engage with multiple target companies to assess attractiveness
- Enter into non-binding LOI to initiate due diligence – non-binding agreements are not subject to Form 8-K disclosure requirement
- As part of diligence process, select investors are "wall crossed" to gauge investor interest
- Begin definitive documentation
- Arrange PIPE and/or debt financing
- Board approval for transaction
- Execute definitive merger documentation along with PIPE agreements
- Announce transaction – Form 8-K, press release and investor presentation
- Proxy filing with the SEC – typically takes 2 months from initial filing to final version
- Conduct roadshow to educate investors about investment opportunity

Closing

- Schedule shareholder vote (sometimes as short as 10 days following mailing proxy statement but longer period often needed to ensure sufficient time to reach retail investors)
- Shareholder vote to approve transaction and related corporate actions
- At closing of the business combination and after payments to redeeming stockholders, the cash in the trust account is released to the surviving company

Current de-SPAC Trends

The landscape is highly dynamic and changes rapidly

Prices have been depressed

- Leads to arb funds coming into the stock, looking for the yield between the trading price and the trust value
- This leads to higher redemption rates
- Higher redemption rates make it more difficult to meet minimum cash conditions

Bridging the Gap: Different Structures

- Sell the Story
- Offer economics from the SPAC sponsor or the target to induce non-redemption agreements
- Structured products (convertible notes; funded forward purchase agreements)

Be aware of timing considerations

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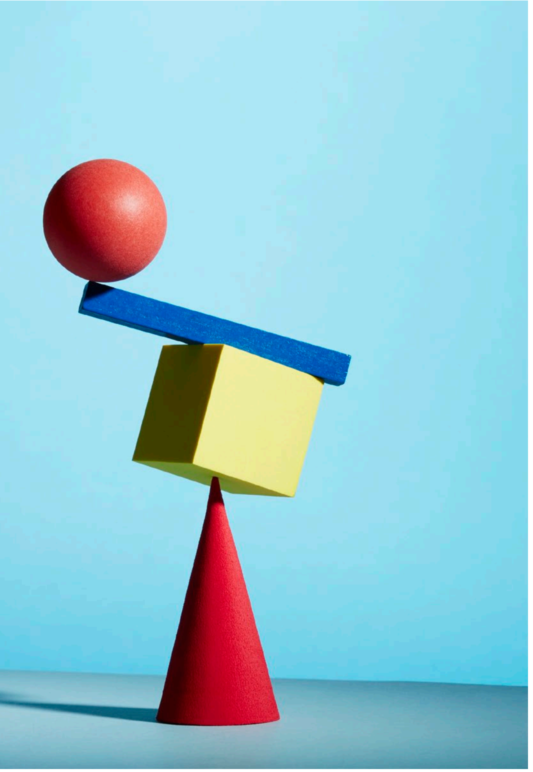
Current Litigation in the SPAC Market

SPAC Litigation: Takeaways

Mitigating Risks

- Be cognizant of the timeline
- Conduct robust diligence
- Observe corporate formalities
- Use care in SEC filings and public statements.
- Address potential conflicts

Timing and Types of SPAC Litigation



- **Pre-closing**
  - Strike suits: disclosure-based claims challenging adequacy of proxy
- **Post-closing**
  - Shareholder suits for breach of fiduciary duty
  - Securities class actions
  - SEC enforcement actions
- **Other suits:**
  - Derivative suits alleging SPACs are investment companies under the Investment Company Act of 1940

Breach of Fiduciary Duty

- **Summary**: Shareholders sue the SPAC, its directors/officers, and its sponsor for breach of fiduciary duties related to the de-SPAC transaction.
- **Key theory**: sponsor and directors incentivized to do ***any*** deal regardless of stockholder interests and did not necessarily choose the ***best*** deal for the SPAC stockholders.
  - Lack of independent committee & sponsor conflicts in light of promote, founder units, warrants
  - Lack of diligence including as a result of external time pressures
    - ***Directors rushing into a business combination to meet de-SPAC deadline***
      - *Laidlaw v. Acamar Partners Acquisition Corp.*, Case No. 2021-0016-SG (Del. Ch. Jan. 7,2021).
    - ***Sponsors entering into a business combination so they could move on to their next SPAC***
      - *Pels, et al. v. FinTech Acquisition Corp, IV*, Case No. 2021-0184 (Del. Ch. Mar 02, 2021).
- Standard of Review: Business Judgment Rule or Entire Fairness
  - SPAC model ***creates inherent conflicts of interest between sponsors and public shareholders*** due to sponsor's interest in founders shares, which are worthless if a deal is not completed.
    - *In re Multiplan*, No. 2021-0300-MTZ (Del. Ch.) (motion to dismiss heard on September 20, 2021)
    - *AP Services, LLP v. Lobell*, 2015 WL 3858818, at *6 (N.Y. Sup. Ct. 2015) (denying motion to dismiss because founders' shares create interests that "deviate[] from that of the stockholders")

Securities Fraud Class Actions

- SPAC or post-SPAC stockholders sue SPAC, sponsor, and directors/officers for misstatements or securities fraud in de-SPAC proxy materials
- **Key theory**: SPAC made a material misstatement or omitted to state a material fact in the proxy materials
    - **§ 10(b) of the Exchange Act and Rule 10b-5:** material misstatements or omissions with scienter
    - **§ 14(a) of the Exchange Act and Rule 14a-9:** material misstatements or omissions but most likely only requires *negligence*. *Beck v. Dobrowski*, 559 F.3d 680, 682 (7th Cir. 2009).
    - **§ 11 of the Securities Act**: strict liability claims under Section 11 where de-SPAC requires registration statement
    - **§ 15 of the Securities Act and § 20 of the Exchange Act**: control person liability
- SPAC and target should be careful with public statements before and after announcement
    - *Churchill IV/Lucid:* class action against SPAC (CCIV), SPAC's CEO and CFO, proposed merger target (Lucid Motors), and target's CEO for statements target's CEO made pre-signing
    - *In re Akazoo S.A.,* No. 20-cv-1900 (E.D.N.Y.): plaintiffs alleged that SPAC misled investors by, among other things, overstating target's profits and the number of subscribers to the target's music streaming app

SPAC Litigation – Mitigating Risk

- **Be cognizant of the timeline**. Proximity between de-SPAC transaction and the SPAC's expiration date will be heavily scrutinized in any ensuing litigation

- **Conduct robust diligence**. Maintain records of diligence conducted
  - SPAC Board can be held liable for material misstatements or omissions in disclosures related to the Target company. SPAC should verify all material statements to avoid negligence liability.
  - Diligence will provide comfort that disclosure is accurate; also provide protection from claims of breach of duty of care or recklessness-based disclosure violations

SPAC Litigation – Mitigating Risk

- **Observe corporate formalities**: regular board meetings and minutes
- **Use care in SEC filings and public statements**.
  - Include (i) appropriate caveats about the sources of information that the sponsor discloses regarding the target company, and (ii) disclaimers for forward-looking statements and opinions
- **Address potential conflicts:** increased SEC and plaintiff focus
  - Fully disclose potential conflicts of interest so approval by stockholders will be fully-informed and help "cleanse" transaction
    - Include advisors' potential conflicts of interest
  - Obtain a fairness opinion and/or form special committee in the event of a conflict, such as where the SPAC is entering a transaction in which one or more directors sit on both sides..

Thank You

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