

## SPAC-and-Span: A Clean Exit?

### PENpoints

*SPACs can present an appealing alternative exit for a private equity sponsor seeking liquidity for a portfolio company for which a traditional sale or IPO proves challenging.*

While robust M&A and IPO markets have given a private equity sponsor solid options for exiting a portfolio company investment, in some cases selling a company to a publicly traded special purpose acquisition company, or SPAC, can be an appealing alternative. Recent examples include Levy Acquisition Corp.'s \$500 million acquisition of Del Taco; Boulevard Acquisition Corp.'s pending \$879 million acquisition of AgroFresh Inc., a Dow Chemical Company subsidiary; and Burger King's conversion to a public company via a \$1.4 billion merger with a UK SPAC.

### SPAC Basics

A SPAC, which is typically sponsored by an experienced investor and/or management team, raises money in an IPO in anticipation of acquiring an unidentified target company, generally with 20 percent of the SPAC's common stock going to the SPAC sponsor — similar to the carried interest in a private equity fund — and 80 percent to the SPAC's IPO investors.<sup>1</sup> The IPO proceeds are then held in a trust account that can be accessed only to complete such an acquisition. If the SPAC does not complete an acquisition within a specified timeframe (e.g., 21 months), it must liquidate and return the trust proceeds to its IPO investors.

While earlier SPACs required stockholder approval before completing an acquisition, thus creating delay and uncertainty, more recent U.S. SPAC structures do not call for a stockholder vote (unless such a vote is otherwise required by law or by stock exchange rules, e.g., upon issuance of more than 20 percent of the SPAC shares as merger consideration), but rather allow the SPAC's stockholders to elect to redeem their shares for cash upon closing of its first acquisition.

### Pros and Cons

*IPO Alternative.* A traditional IPO can be challenging or impossible for certain potential target companies, e.g., because the company is too small or its business is in a down cycle, the equity markets are not open to an IPO or the IPO process is simply too burdensome. In such cases, merging the target company with an already-public SPAC can serve as an alternative to a traditional IPO. Merging with a SPAC also offers

structuring flexibility not available in a traditional IPO, such as earn-outs, escrows and other private M&A methods of allocating risk and upside. In addition, a SPAC merger can be structured so that the target's stockholders retain varying degrees of post-closing control, as well as some upside through partial stock consideration.

*Post-Acquisition Trading.* Transitioning to a normal operating company with a traditional stockholder base trading on the basis of the target's fundamentals — a/k/a “de-SPACing” — can be a challenge. Post-merger trading can be thin if too many of the pre-acquisition SPAC stockholders elect to redeem their SPAC stock at acquisition closing, making it difficult to translate subsequent operational success into increased shareholder value. Because trading on NYSE or Nasdaq can be key to increased stock value, some target companies require as a closing condition that the SPAC meet stock exchange listing requirements at closing.

*No Reverse Break Fees.* Unlike a traditional acquisition agreement, the potential for a target to receive deal protection in the form of a reverse break-up fee from the SPAC (e.g., for failure to raise acquisition financing) can be limited due to restrictions on use of the SPAC's trust account cash.

*Uncertainty About Available Cash.* Because a SPAC's public stockholders can elect to have their shares redeemed for cash in connection with a target acquisition, the amount of cash available to pay target stockholders and maintain post-closing target operations is inherently uncertain. As a result, a seller may require a “minimum cash” closing condition or, perhaps more importantly, that the SPAC has committed acquisition financing. For this reason, many SPAC acquisitions include a simultaneous PIPE investment.

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*Motivated Buyer.* Because a SPAC must liquidate if it does not complete an acquisition within a specified period, with the SPAC sponsor receiving nothing — not even with respect to its 20 percent interest — upon liquidation, a SPAC sponsor is highly incentivized to find and complete a transaction before the SPAC’s acquisition deadline.

While this time pressure can provide negotiating leverage to a target, if the SPAC’s stockholders and the market do not view the target as appropriately valued, the SPAC’s stock will not trade into the hands of investors interested in owning target’s stock post-acquisition, and the SPAC’s stock price will not increase above its redemption value. This can lead to a large number of redemptions by SPAC stockholders at the acquisition closing, which can put significant stress on the company’s post-acquisition capitalization and, in some cases, cause the failure of “minimum cash” or other closing conditions. To avoid this outcome, the terms of the acquisition and/or the SPAC sponsor’s economics are sometimes renegotiated between signing and closing to make target’s stock more attractive to investors (e.g., by reducing the acquisition purchase price and/or the SPAC sponsor forfeiting a portion of its SPAC stock).

*Timeline and SEC Filings.* Eliminating the historical SPAC stockholder vote requirement does not fully

avoid SEC filing requirements with respect to a target acquisition. Because a SPAC is a public company subject to ‘34 Act requirements and SPAC terms require a redemption option for its stockholders — essentially a self-tender offer — the SPAC’s acquisition of the target will involve SEC filings. The related tender offer documents (and proxy statement, should a stockholder vote be required) must include audited financials and full business description of the target, so the target must be “IPO-ready” in order to avoid significant incremental delay. As a result, a SPAC acquisition typically takes three to five months to complete, generally comparable to a traditional IPO, but likely longer than a private sale.

While the recent improved track record for SPACs has eliminated much of the reputational taint associated with earlier “shell company” structures, some private equity sponsors remain wary of selling a portfolio company to a SPAC because of the associated complexities compared to more traditional market exits. Nevertheless, SPACs present an interesting alternative exit for a private equity sponsor, especially when chop-piness in the IPO market or where lack of acquisition capital for buyers makes the traditional M&A market comparatively less attractive.

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1 Actually, the 20 percent to the SPAC sponsor is economically better than the 20 percent carried interest to a private equity fund’s sponsor because the latter is an interest only in appreciation while the former is an interest in SPAC capital as well as appreciation.

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If you have any questions about the matters addressed in this *KirklandPEN*, please contact the following Kirkland authors or your regular Kirkland contact.

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## Update on BEA’s Survey of U.S. Overseas Investment

Over the past several months, private fund managers with at least one direct or indirect 10 percent-or-greater voting interest in a non-U.S. entity have worked to complete reports required by the U.S. Department of Commerce, Bureau of Economic

Analysis (“BEA”) for its benchmark survey of U.S. overseas investment. Inundated with questions as the original May 31, 2015, deadline approached, the BEA automatically extended the deadline for all first-time filers to June 30, 2015.

At about the same time, however, the BEA reversed its policy (described in our prior [PEN](#)) of accepting so-called “deconsolidation requests” that allowed a private equity firm to avoid consolidating all the information from its various U.S. portfolio companies simply because the fund or one such U.S. portfolio company had a 10 percent-or-greater voting interest in a non-U.S. entity.

Since then, many private fund managers have sought a filing extension, which the BEA has granted as a matter of course. The current filing deadlines for anyone with an extension are (1) **August 31, 2015**, for submission

of reports relating to non-U.S. entities and (2) **October 31, 2015**, for submission of the report consolidating the activities of all its U.S. entities.

As a reminder, a U.S. entity must file a BE-10 Benchmark survey report if it owned, directly or indirectly, 10 percent or more of the “voting stock” of a non-U.S. entity at any time during 2014. How this requirement applies to a particular U.S. private fund fund sponsor (including one with multiple funds) is a complex question depending on a number of variables, including its structure and other facts and circumstances.

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## PENnotes

**Structuring and Negotiating LBOs**  
**San Francisco, CA**  
**September 10, 2015**  
**New York, NY**  
**September 24, 2015**  
**Chicago, IL**  
**October 1, 2015**

This biennial event, chaired by Kirkland partner Jack Levin, focuses on the legal, tax, structuring and practical negotiating aspects of buyouts and other complex private equity deal-doing. More information to follow.

**PLI Hot Topics in Mergers & Acquisitions 2015**  
**Chicago, IL**  
**September 16, 2015**  
**New York, NY**  
**October 2, 2015**

An expert faculty of lawyers, general counsel, regulators and investment bankers will explore the state of M&A and trends for the year ahead. Kirkland partners Scott Falk and Sarkis Jebejian are co-chairs of the event. Click [here](#) for more information.

**Securities Filings 2015: Practical Guidance in a Changing Environment**  
**Chicago, IL**  
**November 12-13, 2015**

This program will analyze in detail the principal forms used for filings with the SEC under the Securities Act of 1933, and the Securities Exchange Act of 1934, with particular emphasis on the mechanics of and timing for assembling particular filings. Recent legislation and SEC rule changes affecting disclosure obligations, in particular those resulting from the JOBS Act, will be woven within the topics covered. Kirkland partner Carol Anne Huff will speak at the event. Click [here](#) for more information.

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Kirkland & Ellis' nearly 400 private equity attorneys have handled leveraged buyouts, growth equity transactions, recapitalizations, going-private transactions and the formation of private equity, venture capital and hedge funds on behalf of more than 400 private equity firms around the world.

Kirkland has been widely recognized for its preeminent private equity practice. The Firm was named "Private Equity Group of the Year" in 2012, 2013 and 2014 by *Law360* and was commended as being the most active private equity law firm of the last decade in *The PitchBook Decade Report*. Kirkland was named "Law Firm of the Year in Mergers and Acquisitions Law" by U.S. News Media Group and Best Lawyers in its 2014 "Best Law Firms" rankings. The Firm was named "Best M&A Firm" at *World Finance's* 2014 Legal Awards, "North American Law Firm of the Year: Fund Formation" and "North American Law Firm of the Year: Transactions" at *Private Equity International's* 2014 Private Equity International Awards and "Private Equity Deal of the Year" at the 2014 IFLR Americas Awards.

In 2012, 2013 and 2014, Chambers and Partners ranked Kirkland as a Tier 1 law firm for Investment Funds in the United States, United Kingdom, Asia-Pacific and globally. The Firm was ranked as the #1 law firm for both Global and U.S. Buyouts by deal volume in Mergermarket's *League Tables of Legal Advisors to Global M&A for Full Year 2011, 2012, 2013 and 2014*, and has consistently received top rankings among law firms in Private Equity by The Legal 500 and IFLR, among others.

*The Lawyer* has recognized Kirkland as one of its "Transatlantic Elite" every year since 2008, having noted that the Firm is "leading the transatlantic market for the provision of top-end transactional services ... on the basis of a stellar client base, regular roles on top deals, market-leading finances and the cream of the legal market talent."

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