Vinson&Elkins

The Rise of the SPAC

Presentation to

Women Corporate Directors (Houston)

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Introductions

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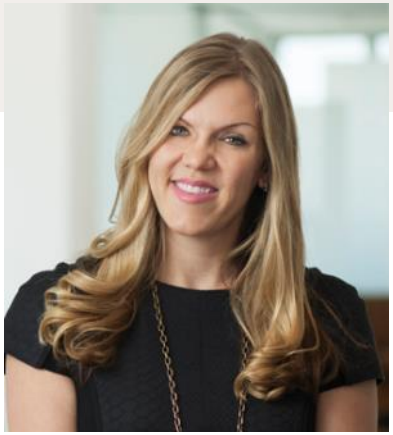

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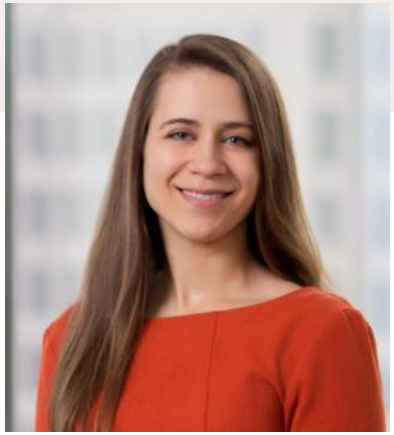

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Today's Discussion

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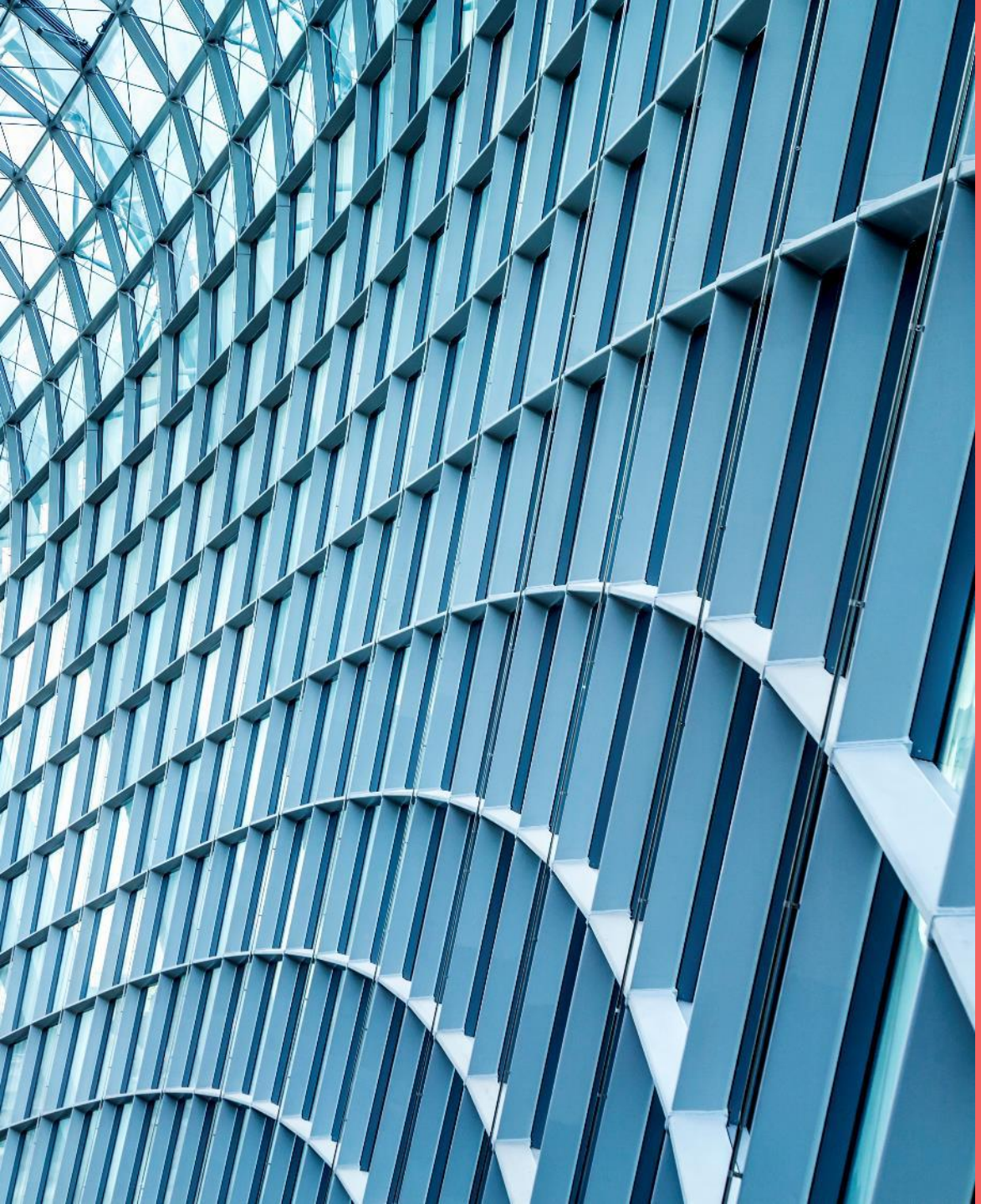


SPAC Introduction

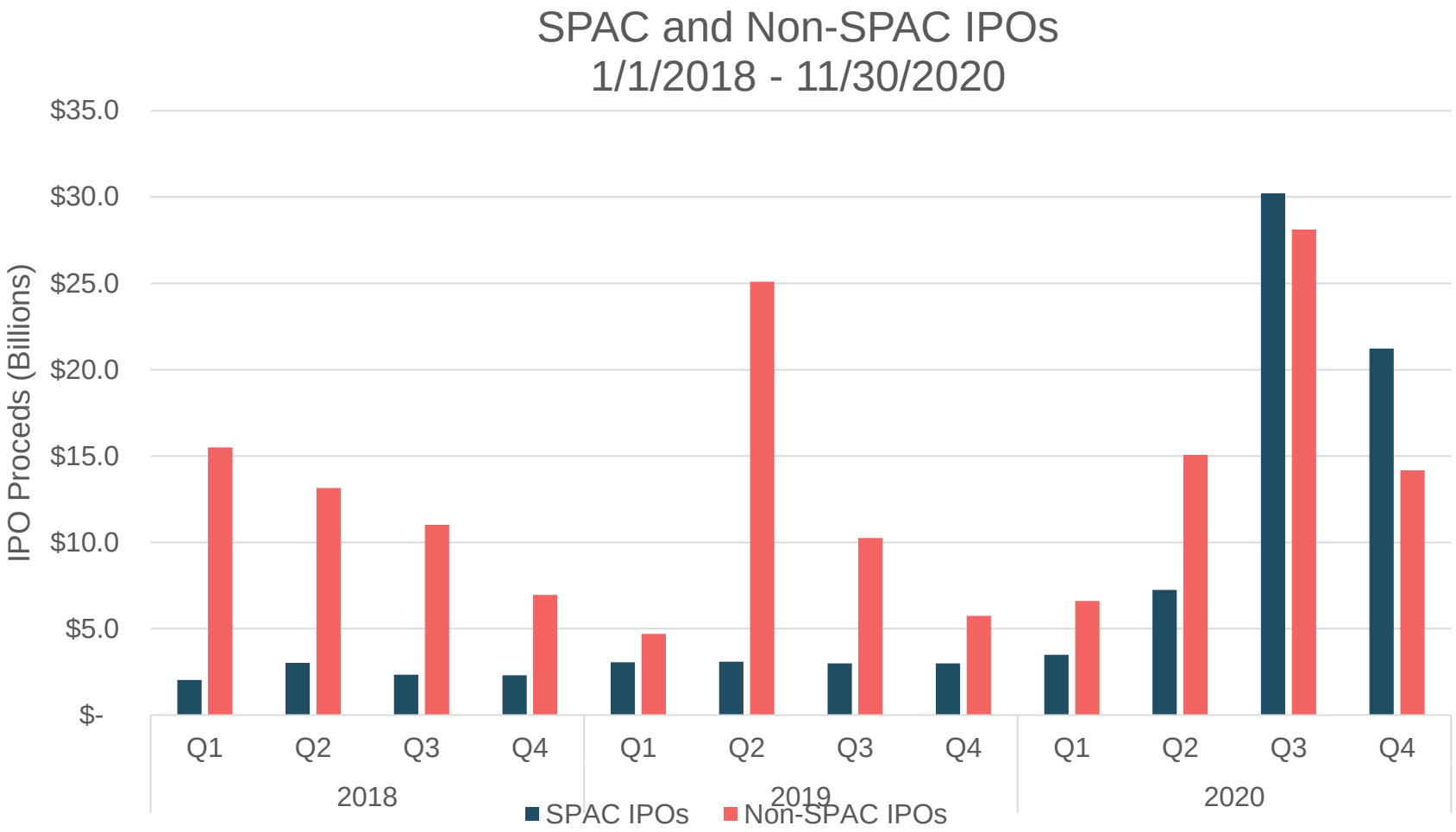
What's a SPAC

- Special Purpose Acquisition Companies ("SPACs") are companies formed to raise capital in an initial public offering ("IPO") with the purpose of using the proceeds to acquire a business or assets to be identified after the IPO.
- Illustrative SPAC structure:
  - Class B shares or founder shares issued to Sponsor for a nominal amount (aka the "promote") and equal 20% of total shares outstanding after IPO
  - Sponsor purchases private placement or founder warrants (aka the "at-risk capital") the proceeds of which will cover a portion of the UW discount and the SPAC's expenses
  - Units consisting of a Class A share and a portion of a warrant issued to the public in the IPO for $10 per unit; public shares equal 80% of total shares outstanding after the IPO
  - IPO proceeds are deposited in a trust account until De-SPAC transaction or SPAC's liquidation
- Generally a SPAC has two years to acquire a target otherwise it liquidates and the trust proceeds are returned to the public shareholders

What's a De-SPAC

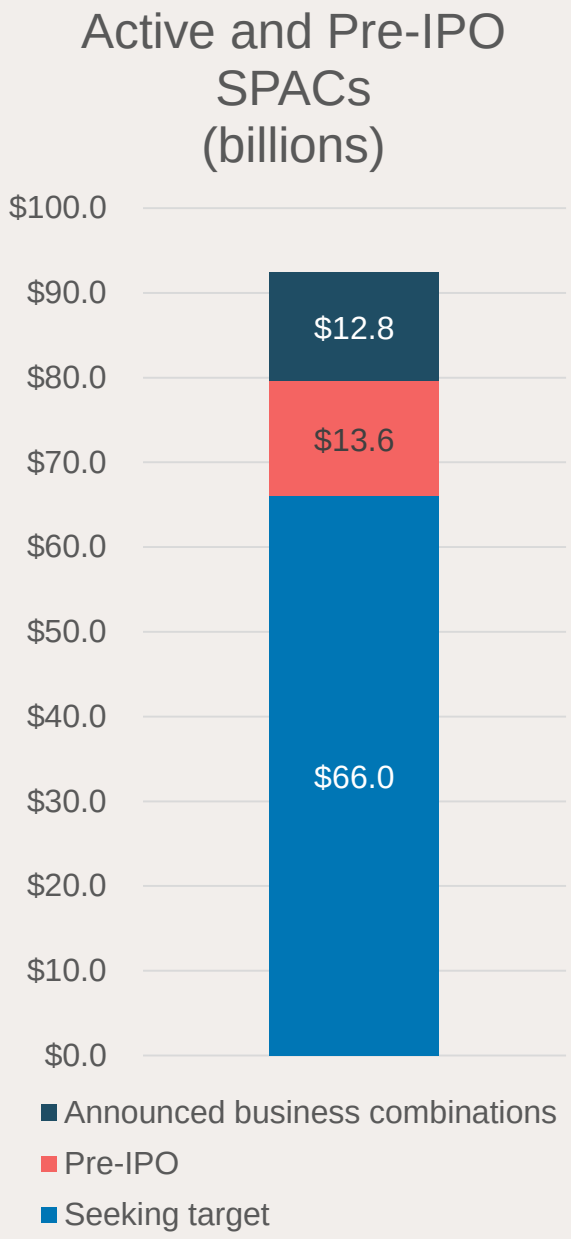
- The business combination between a SPAC and the target company is often referred to as a "De-SPAC" or "De-SPAC transaction"
- A De-SPAC transaction can be used as:
  - Financing – where the trust proceeds are used to finance growth (or de-lever)
  - Liquidity – where the trust proceeds are used to cash out the target's owners
  - Combination
- Typically three main aspects to a De-SPAC transaction:
  - Public company merger
  - PIPE financing
  - Proxy/registration statement (Form S-4/F-4)
- Average six months from letter of intent to closing business combination

SPAC IPO Activity
(through 11/30/2020)

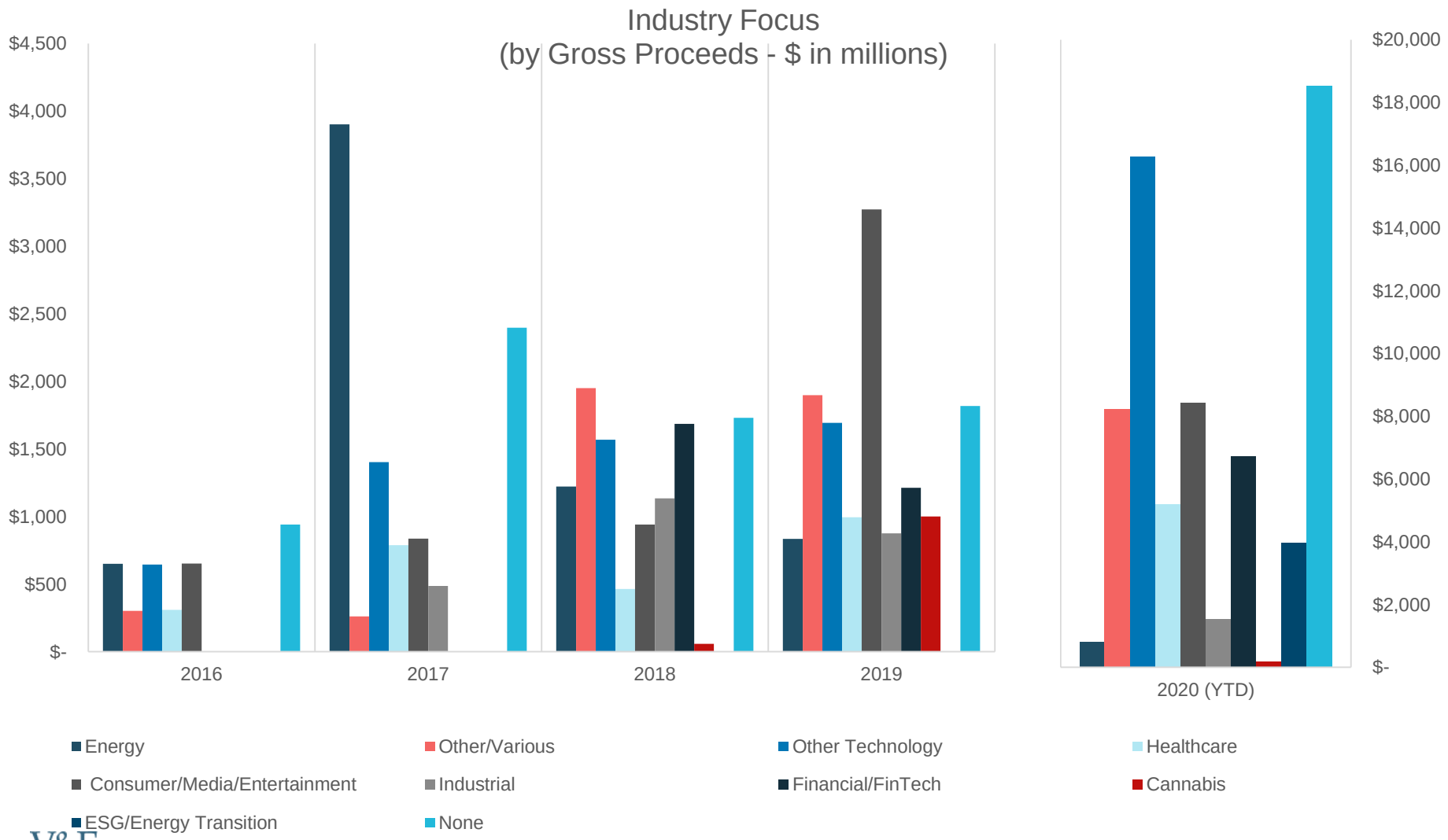


Active/Pre-IPO SPACs
(as of 12/1/2020)

- 251 Active SPACs, with ~$78.8 billion in trust
  - 51 announced business combinations, representing $12.8 billion
  - 200 hunting, with $66.0 billion in trust
- 58 IPOs in registration publicly filed, with current fee tables indicating ~$13.6 billion will be raised



SPAC Industry Focus at IPO



SPACs in 2020

- Developments
  - Increased acceptance by investors
    - Retail investors' increased interest in the stock market has generally also applied to SPACs
    - Increased participation by long-only institutional investors
  - Diversification of Sponsors
    - Larger PE firms, activist funds and high-profile individuals
    - Public company
  - Adjustments and innovations to the SPAC structure
    - Warrants
    - Sponsor economics
    - Up-SPAC structure
  - Private companies have started to proactively prepare for a possible De-SPAC transaction

DeSPAC Process and Directors' Role and Responsibilities

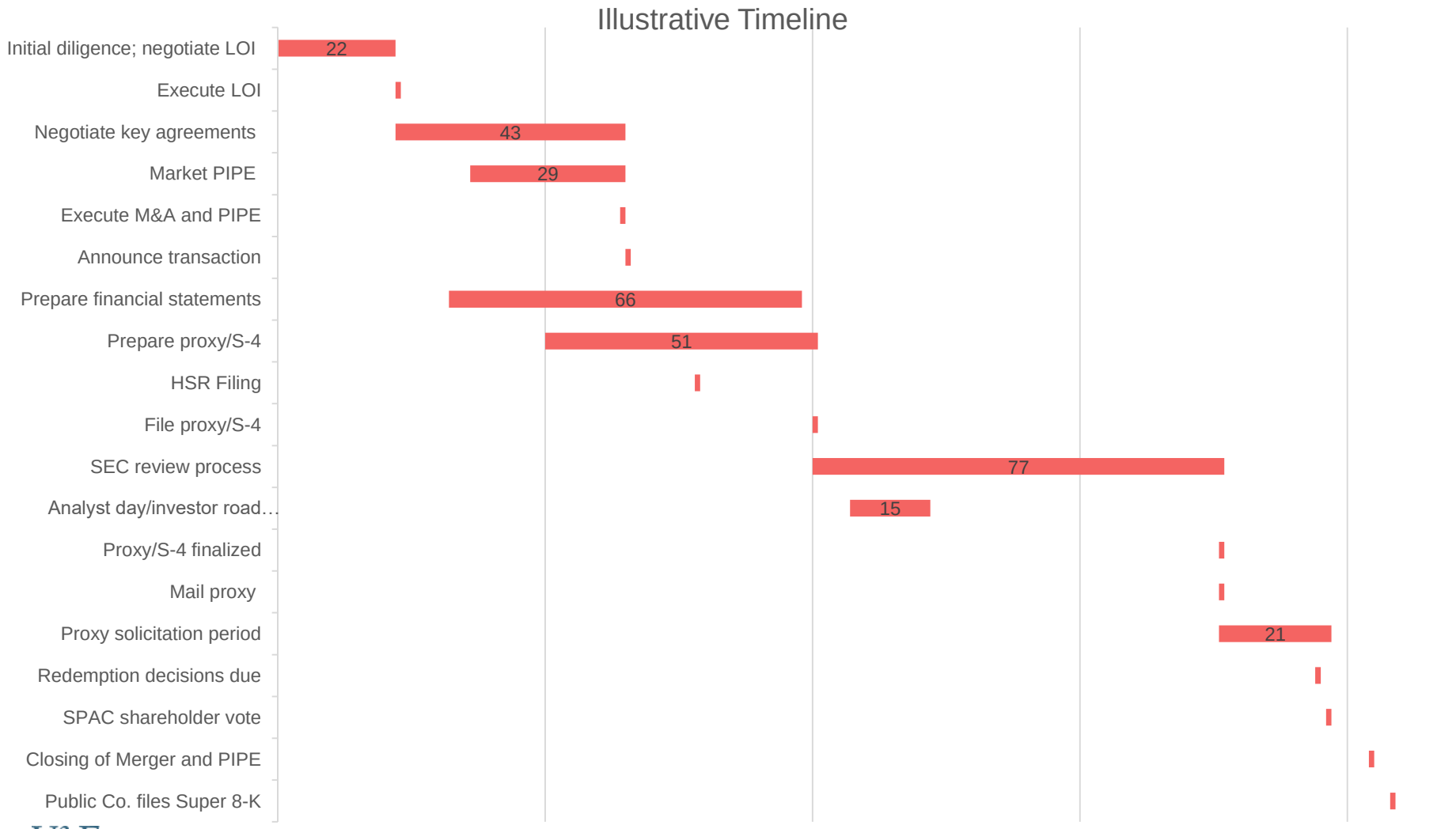
SPAC Directors at SPAC IPO

- Selection
  - Directors of the SPAC are selected by the sponsor at IPO, most recently typically before testing the waters process in order to inform potential investors of BOD
  - Sponsors will want independent directors with experience and reputations to assist in identifying and evaluating targets for a business combination, typically with experience/relationships in the chosen target industry of the SPAC
- Governance Structure
  - SPACs are required to have a majority of independent board members and independent committees under NYSE/NASDAQ listing requirements, subject to the same phase-in exceptions as are applicable to all newly public companies.
    - Practically speaking, audit committee services perfunctory given SPAC's lack of operations and limitations on what can be done with trust capital; similarly no real role for compensation or nom/gov. committee
    - SPAC directors' primary duties relate to evaluating business combination transaction
  - In most instances, a SPAC will not hold a public election for directors until the De-SPAC transaction or thereafter, and some SPACs provide that only the founder shares vote in director elections until the De-SPAC transaction.

SPAC Directors at SPAC IPO

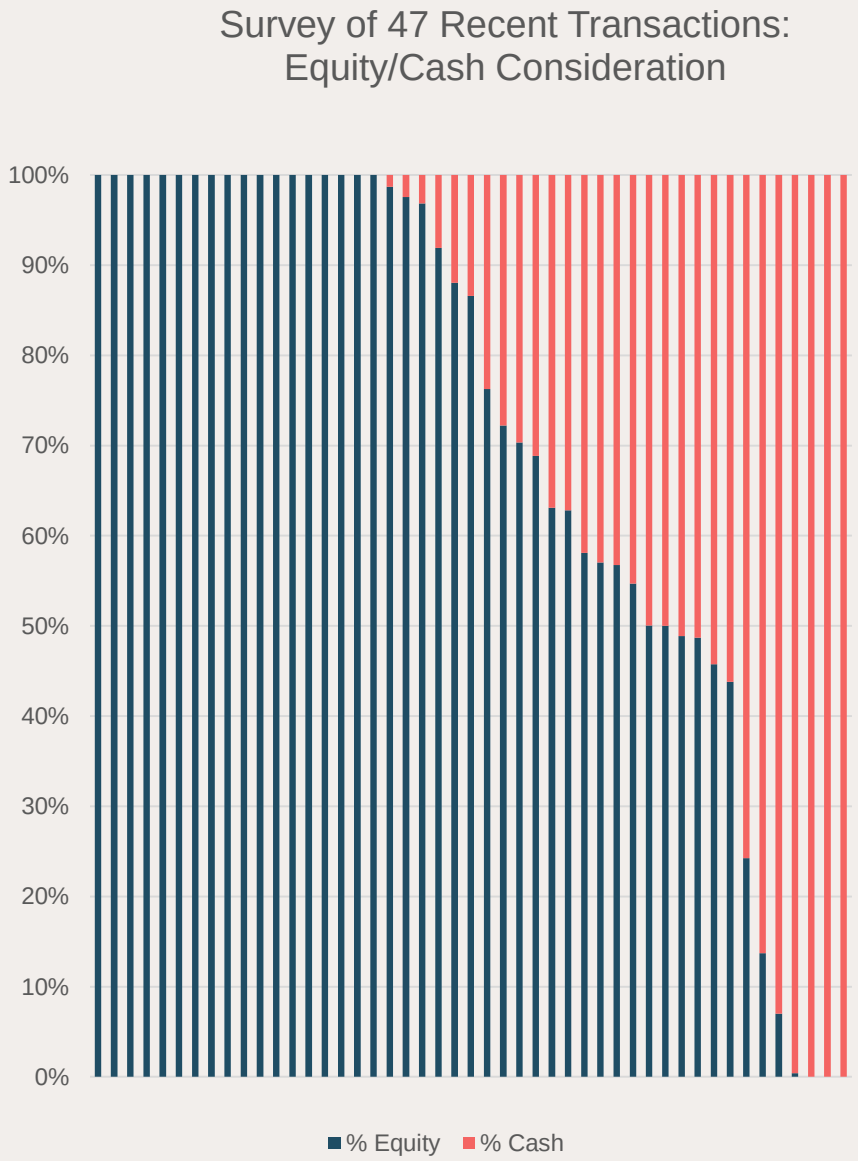
- Compensation
  - Independent directors are typically compensated for their service through transfer of founders shares from sponsor
  - Sometimes independent directors are invited to fund at risk capital for Sponsor

Overview of De-SPAC Timeline and Process



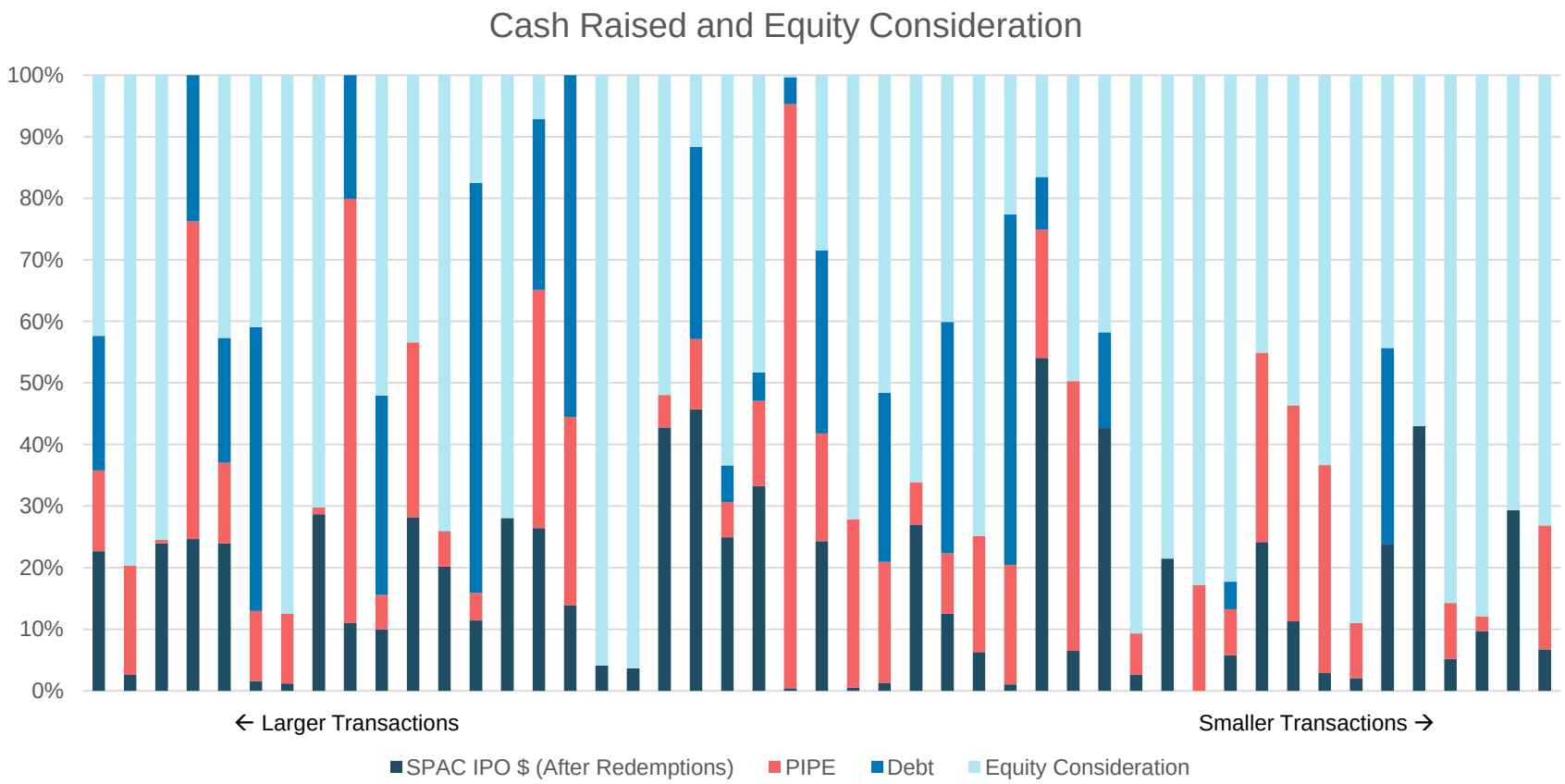
Cash/Equity Consideration For Target Equityholders

- For the private company (commonly referred to as the “target”), a De-SPAC can serve as:
  - a financing
  - a liquidity/exit event
  - a mix of both
- In financing transactions, existing equityholders roll equity, and cash is retained by the company for future growth, deleveraging, etc.
- In liquidity/exit transactions, existing equityholders receive more cash, and management may be replaced
- Recent transactions surveyed have skewed to the financing end of the spectrum, and PIPE and SPAC investors prefer all equity transactions



Financing

- SPAC IPO (net of redemptions – note that redemptions are a variable until 2 days before the vote)
- Equity or debt (including to backstop redemptions)
- Seller equity consideration

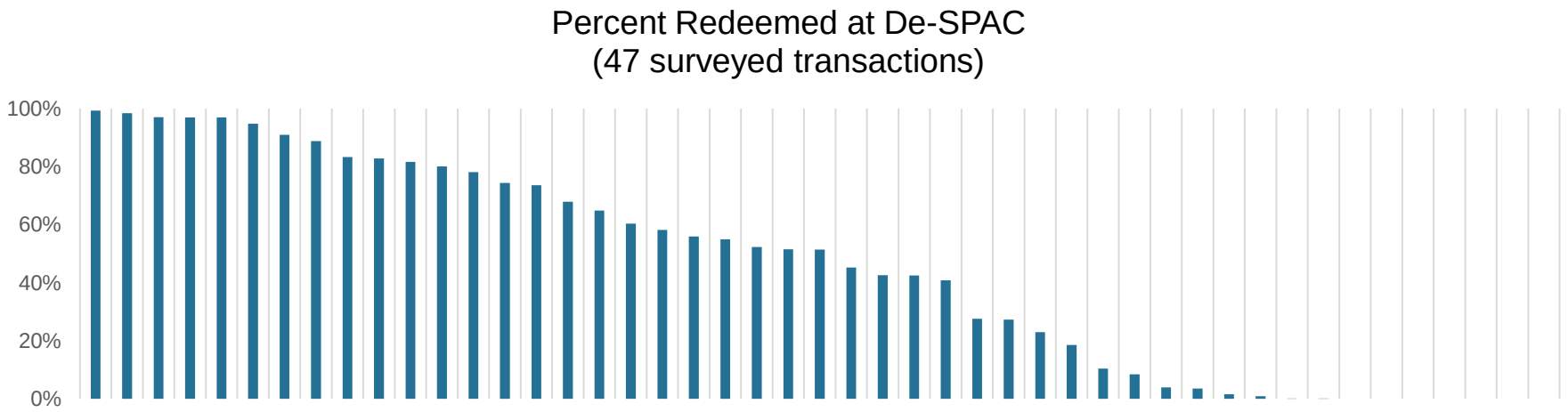


Proxy/S-4

- SPAC will usually be required to produce a proxy statement to seek shareholder approval and offer redemption rights to SPAC shareholders
  - a proxy may be combined with a registration statement on Form S-4 (or F-4) because (i) the issuance of merger consideration to target shareholders usually requires registration under U.S. securities laws or (ii) the SPAC is not the surviving company
  - in rare circumstances a tender offer may be permitted in lieu of a proxy solicitation
- The proxy (or registration statement) is a disclosure document describing the target and De-SPAC
  - preparation joint SPAC and target effort
- Information is substantially similar to information required in IPO registration statements
  - SEC requires PCAOB audited financials of target to be included
  - unlike IPO registration statements, multi-year projections generally required due to SPAC Board approval process
  - disclosure in proxy vs. a registration statement is generally similar, but a registration statement introduces additional complexities and securities law liability

SPAC Redemption Rights

- SPAC stockholders must be provided with the opportunity to redeem their shares in connection with the De-SPAC
  - decision made 2 business days before vote
- Redemption price = ~pro rata share of amount then in the SPAC trust account
  - stockholders can redeem irrespective of whether they vote for or against the transaction: stockholder vote typically not a concern – redemptions are the key focus
- If trading price at the redemption date is above the redemption value (pro rata trust amount per share), SPAC shareholders who dislike the deal should sell rather than redeem
  - retail ownership may change dynamic, and T+2 settlement may result in non-redeemable shares



SPAC Directors – DeSPAC Process

- Post-IPO, periodically meet with SPAC management to discuss potential targets/process of seeking targets.
- Once target selected, meetings with SPAC management to review proposed deal terms, diligence process and valuation information and ultimately approve business combination.
  - As with any public M&A, board process and projections relied upon by the board will be detailed in “Background of the Merger” in the proxy/ registration statement.
- Limited SPAC director involvement once business combination is signed unless there is a need to recut the deal post-signing.

SPAC Directors – Fiduciary Duties

- Fiduciary duties of directors of a DE SPAC no different than regular DE Corp
- **Fiduciary Duties** –Directors are fiduciaries of the stockholders and owe them principally (1) a duty of care and (2) a duty of loyalty.
  - **Duty of care** involves an examination of whether directors have adequately informed themselves, before making a business decision, of all material information reasonably available to them.
  - **Duty of loyalty** involves an examination of whether a director stands on both sides of a transaction or derives any personal benefit through self-dealing
    - A director must not consider or represent interests other than the best interests of the corporation and its stockholders in making a business decision
- **Other (embedded) duties:** oversight, good faith, disclosure, and candor

Potential Liability for SPAC Directors

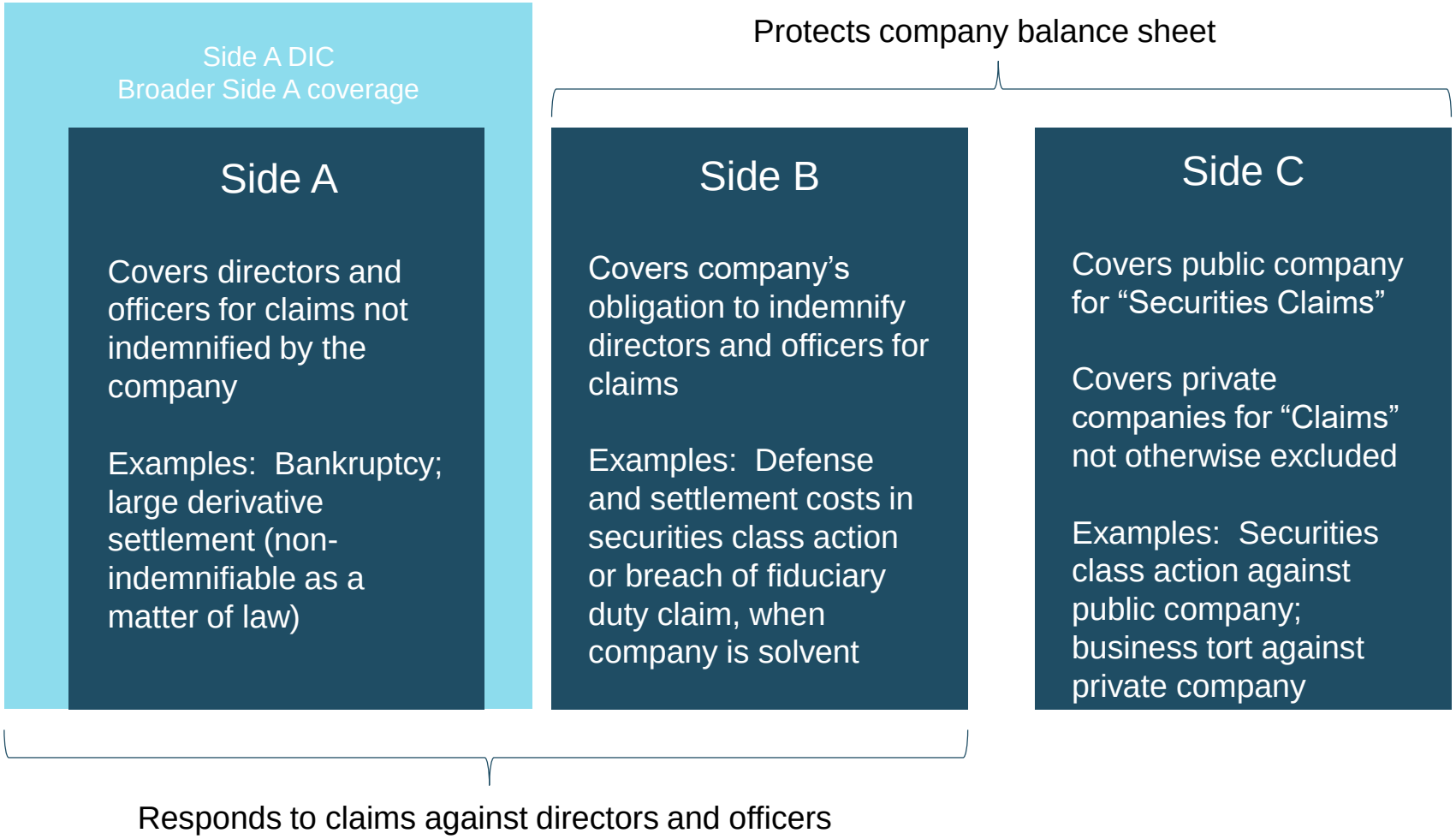
- **Breaches of Fiduciary Duties**
  - Business Judgement Rule typically applies to non-conflicted transactions; lenient standard
  - Entire Fairness applies where majority of the board has a material conflict; requires defendants establish underlying transaction was product of fair dealing and fair price.
    - *NY Trial Court* found that SPAC structure ("founders shares" and "ticking clock") inherently renders SPAC board members as conflicted; DE courts have not weighed in yet
    - Even if Board finds conflict, *Corwin* doctrine says board can avoid entire fairness review if they can demonstrate conflicted actions ratified by ***fully informed*** vote of disinterested shareholders
  - ***Key Takeaway – very important to have robust disclosures of all conflicts***
- **Federal Securities Laws Claims**
  - In the "de-SPAC" transaction, when a SPAC acquires its target, the SPAC and its sponsors are potentially liable under the Securities Exchange Act of 1934 for misleading statements included in a proxy statement or in other public statements or Securities Act of 1933 if that de-SPAC transaction includes a registered offering.
  - Investors have sought to hold SPACs and their sponsors, officers and directors liable for a variety of alleged misstatements, including about the financial outlook of the target companies and the level of due diligence performed by the SPAC.
  - ***Key Takeaway***: ***the best ways to mitigate these risks are to perform sufficient due diligence on the target and to be cautious with language in the proxy statement.***

SPAC Directors Post De-SPAC

- Seller and SPAC Sponsor generally seek to maintain representation on the board following the deSPAC transaction until they have sold down their stake in the company by entering into shareholder agreements in connection with the deSPAC transaction that give Seller and SPAC Sponsor the right to select initial board and also to nominate directors to stand for election following the deSPAC
  - In recent transactions, very typical for Sellers to take a significant amount of equity consideration in the new public company for sale of target (vs cash) and as a result Seller often has large or even controlling position in new public company and the right to several director designees under the shareholders agreement
  - Conversely – after equity issued to the target and PIPE equity issuances, the SPAC sponsor typically ends up with 5-10% of the public company, and often only has the right to one (and sometimes no) director under the shareholders agreement.
    - Typically fill this seat with sponsor affiliated director
  - As a result it is unusual for the SPAC independent directors to continue as directors of the company post-business combination

D&O Insurance

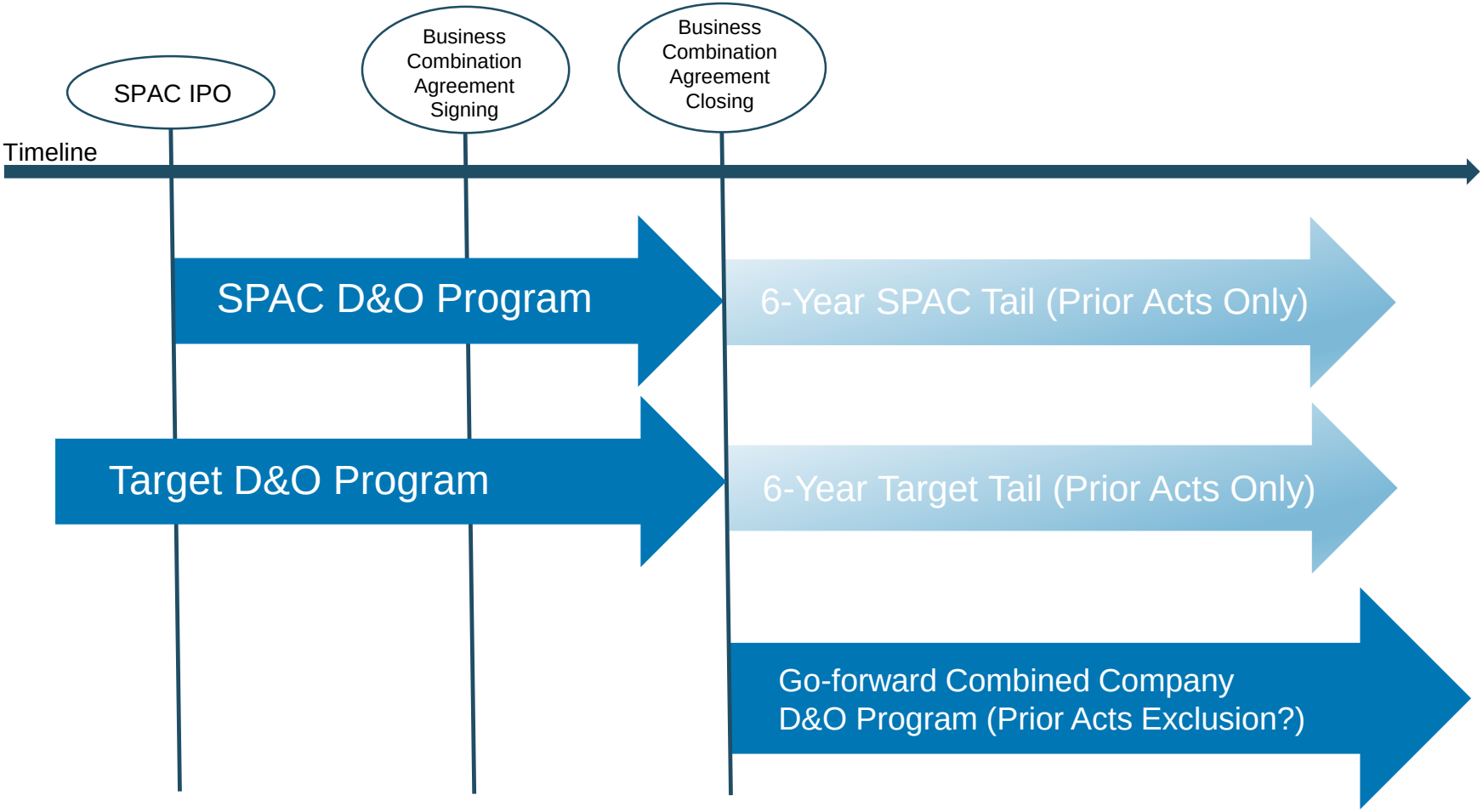
What does D&O insurance cover?



Best Practices for SPAC D&O Program at Initial IPO

- Obtain the “right” amount of D&O insurance for the “best” premium
  - Work with an experienced broker and outside counsel to evaluate options.
  - Broker can provide peer benchmarking to assist in considering appropriate limits.
  - Don’t automatically choose the lowest premium quoted; consider terms offered by each underwriter, including retention and key exclusions.
    - Avoid any prior acts exclusion.
    - Pre-negotiate 6-year tail premium.
  - Premiums for SPACs have skyrocketed.
    - Market capacity is limited. Only 5-6 underwriters issue D&O policies in this space.
    - Pressure should ease slightly in early 2021, but premiums will still be high.
- Obtain the right mix of D&O insurance products
  - Consider at least one layer of Side A DIC coverage, in addition to traditional Side ABC policies.

De-SPAC Transaction: D&O Insurance Considerations



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