

SPAC Talk: Important Considerations for Private Companies Evaluating a SPAC Going-Public Transaction

April 7, 2021 – Cross-Border Counselor

by Christopher L. Doerksen and Randal R. Jones

One of the hottest going-public trends in 2020 and 2021 has been the rise of SPACs – Special Purpose Acquisition Companies – as a vehicle for private companies to go public. SPACs are shell companies that are formed, funded and taken public for the purpose of later acquiring an operating company. By merging with a SPAC, the private company effects a reverse takeover, inheriting the SPAC's existing cash and taking over its management. SPAC mergers have quickly increased from being occasional to outpacing the number of traditional IPOs.

A SPAC merger involves different players that can have different motivations than a traditional IPO. In a traditional IPO, a private company may slowly prepare to become a public company, augmenting staffing and systems over a period of years, before engaging with underwriters that will conduct an initial public offering of securities for the company. By comparison, in a SPAC merger, the SPAC typically has a limited window of time, usually 12-24 months, in which it can identify, negotiate and close a qualifying transaction. Failure to complete a transaction by the end of that period requires the SPAC to return capital to its investors. This limited timeframe puts great pressure on the private company to be ready to go public more quickly. In addition, the SEC imposes certain disabilities on successors to SPACs.

On March 31, 2021, the SEC issued two new guidance documents highlighting these and other important issues that a private company should consider before going public by merging with a SPAC.

First, the SEC's Division of Corporation Finance issued a [Staff Statement on Select Issues Pertaining to Special Purpose Acquisition Companies](#), which reminds private companies that if they go public through a SPAC merger, the combined public company will be subject to a number of special rules applicable to former shell companies, which include:

- Financial statements for the acquired business satisfying the SEC's standards must be filed within four business days of the completion of the merger, as part of a larger

Related People

- Christopher L. Doerksen

Related Capabilities

- Canada Cross-Border Transactions

filing that must include extensive additional information regarding the combined business, similar to the information that would be required in an SEC registration statement or prospectus (referred to as Form 10 information);

- The combined public company cannot use incorporation by reference in a Form S-1 registration statement for three years after the completion of the merger;
- The combined public company cannot use Form S-8 to register compensatory securities offerings until at least 60 days after the combined company has filed current Form 10 information;
- The combined public company will be an “ineligible issuer”, as defined by the SEC, which means that for three years following the completion of the merger, the issuer:
 - Cannot qualify as a well-known seasoned issuer;
 - May not use a free writing prospectus;
 - May not use a term sheet free writing prospectus available to other ineligible issuers;
 - May not conduct a roadshow that constitutes a free writing prospectus, including an electronic roadshow; and
 - May not rely on the Rule 163A safe harbor, which protects certain pre-filing communications from being considered impermissible offers of securities;
- The combined public company will be subject to the Exchange Act’s requirements relating to adequate books and records, internal control over financial reporting and disclosure controls and procedures; and
- If the SPAC was listed on a national securities exchange, such as the New York Stock Exchange or NASDAQ, the exchange will require the combined public company to satisfy all quantitative and qualitative standards applicable to an initial listing in order to remain listed after the merger.

Further, while not mentioned in the Staff Statement, Rule 144 is not available to permit resales of securities of a former shell company until one year after the resulting issuer has filed current Form 10 information, and thereafter, its availability is always conditioned upon the combined public company continuing to be an SEC reporting company that is current in its SEC filings.

Concurrent with the Staff Statement, Paul Munter, the SEC’s Acting Chief Accountant, issued a public statement on Financial Reporting and Auditing Considerations of Companies Merging with SPACs. This statement highlights a number of things for private companies to consider before completing a SPAC merger, generally seeking to impress upon private companies that a SPAC merger should be approached with the same seriousness, planning and rigor as a traditional IPO:

- **Marketing and Timing Considerations.** While a private company may spend years preparing for a traditional IPO, SPAC mergers are often sought to be completed within a few months. It is, therefore, essential that target companies have a comprehensive plan in place to address the resulting demands of being a public company on an accelerated timeline. This includes preparing for robust financial reporting and filing requirements, as well as an evaluation of various functions, including people, processes and technology, that will need to be in place to meet SEC filing, audit, tax, governance and investor relations need post-merger. It is essential for the combined public company to have a capable, experienced management team that understands what the reporting and internal control requirements and

expectations are of a public company and can effectively execute the company's comprehensive plan on an accelerated basis;

- **Financial Reporting Considerations.** The combined public company should have sufficiently knowledgeable personnel, appropriate staffing and processes in place to produce high quality financial reporting that is in compliance with all SEC rules and regulations. Management should be prepared for various financial reporting challenges that may arise in the process of the SPAC merger, including complex accounting issues such as the determination of the appropriate accounting principles, identification of the combined company's predecessor entity for financial statement purposes, the form and content of the required financial statements and pro forma information, which entity should be treated as the acquirer for accounting purposes, accounting for any earn-out or compensation arrangements, transitioning from private to public company accounting principles and potential acceleration of adoption of recent accounting standards;
- **Internal Control Considerations.** Management should understand the requirements relating to internal control over financial reporting and disclosure controls and procedures, including the timing of management's first required reports on these topics, and any required auditor attestation of internal control over financial reporting;
- **Corporate Governance and Audit Committee Considerations.** Companies should understand the importance and role of the board and audit committee of each party to the SPAC merger, and the combined public company, including the range of skills, experience and independence of the board of the combined public company; and
- **Auditor Considerations.** The private company's annual financial statements should be audited in accordance with the Public Company Accounting Oversight Board (PCAOB) standards by a public accounting firm registered with the PCAOB and compliant with both PCAOB and SEC independence requirements. This requires thoughtful consideration, and may require changes to previously prepared financial statements, the auditor or the audit team. Auditor independence, in particular, can be an issue in SPAC mergers.

SPAC mergers provide an important alternative to a traditional IPO, but as discussed above, they should be approached with the same seriousness, planning and rigor as a traditional IPO.