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To SPAC or IPO

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A lot has been reported on Special Purpose Acquisition Companies ("SPAC") and their revived use to raise money through an initial public offering ("IPO"). There were 248 SPACs started in 2020 raising approximately $83 billion. As of the beginning of June 2021, approximately 430 additional SPACs were started raising over $100 billion. The use of SPACs does not appear to be slowing down.

Some businesses may consider either going public through an IPO or being acquired via a SPAC. There are pros and cons to each option that should be considered.

As background, a SPAC is a shell corporation that has no business other than to find a target to acquire and merge taking the target public. Investors in a SPAC do not know what business they will ultimately be investing in.

Sponsors that start the SPAC typically make a nominal investment (typically a combination of stock and warrants) but own about 20% of the SPAC. The funds from the sponsors are used to finance the IPO and for working capital purposes. Sponsors maybe private equity or a group of experienced executives.

The investment in the SPAC IPO by investors is usually placed in escrow until the target is identified and the merger is approved by stockholders or if liquidation occurs because a merger with a target was not completed in required time frame.

Typical SPACs have 18 to 24 months to locate a target and close the transaction (merge with the target) taking the target public ("DeSPAC").

What makes SPACs attractive is that they provide a route to take the target company public on a reduced timeline without some of the pricing variations that occur with traditional IPOs. The value of the target is agreed upon between the SPAC and the target. Investors in the SPAC that do not agree with the proposed merger may receive their investment back. Investors also have the right to approve or reject the merger with the target.

The following is a simple chart of some of the differences between a SPAC and a traditional IPO.

	SPAC	**Traditional IPO**
Timeline to IPO	3 to 6 months – review process is deferred until De-SPAC	12 to 18 months – full SEC review process
Price	More price certainty and limited market fluctuations	Full risk including market fluctuations because price is

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		set at IPO
Dilution	SPAC sponsors usually own 20% stake, warrants and earnout	Standard
Redemptions	Shareholders can redeem their shares at any time and if too many redemptions occur, the SPAC may not have the funds needed to De-SPAC	N/A
Underwriting	2% fee to start and 3.5% at completion	6% to 7% underwriting fee
Other	Target company usually bears the brunt of the regulatory filings required by the SEC under a shorter timeframe which can lead to errors and litigation	

If you are a private company considering on going public, either a SPAC or traditional IPO may be an option for you.

For additional information, please contact one of the authors or a member of Masuda Funai's Corporate, Finance & Acquisitions Practice Group.

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