OSLER

SPACs seek to complete qualifying acquisitions

DECEMBER 6, 2016 8 MIN READ

Related Expertise

- Banking and Financial Services
- Capital Markets
- Mergers and Acquisitions

Authors: Douglas Marshall, Jeremy Fraiberg, SPACs seek to complete qualifying acquisitions

The deadlines for completing an acquisition for the special purpose acquisition corporations (SPACs) that were created in a wave in 2015 are approaching. As we commented previously (see Special Purpose Acquisition Corporation (SPAC) offerings: Will we see more?), whether SPACs will continue to be a viable asset class will likely depend on whether this group of initial SPACs is successful in completing a "qualifying acquisition" – an acquisition by the SPAC of a business with the escrowed proceeds of the initial equity offering.

The chart below provides a summary of the deadlines by which each of the 2015 SPACs (and one completed in 2016) must complete its qualifying acquisition:

For each SPAC, the initial deadline may be extended to 36 months after the closing of the initial public offering with shareholder approval and the consent of the TSX, if required. The extended deadline for each of the first four SPACs in the chart applies if the SPAC has executed a letter of intent, agreement in principle or definitive agreement for a qualifying acquisition by the initial deadline. In the case of Kew Media, the initial deadline may be extended twice by three months each time upon the subscription by the sponsor or other founders for $525,000 of units.

To date, four proposed transactions have been announced, although none of these SPACs has yet completed a qualifying acquisition.

INFOR Acquisition Corp. (IAC) announced on July 25, 2016 that it had entered into an arrangement agreement with Element Financial Corporation. The agreement provided for an arrangement of IAC pursuant to which IAC would be acquired by the company carrying on the North American commercial finance business to be spun off from Element. This transaction, which would have been the first completed qualifying acquisition by a SPAC, was terminated by agreement of the parties on October 12, 2016 shortly before the proposed meeting of SPAC shareholders called to consider the transaction.

Dundee Acquisition Corp. (DAC) announced on August 25, 2016 that it had entered into an arrangement agreement with CHC Student Housing Corp. The agreement provides for an arrangement of DAC pursuant to which DAC will be acquired by CHC and the combined entity will acquire certain additional student housing properties. DAC intends to hold a meeting of shareholders on December 20, 2016 with closing of the transaction expected to occur in December.

Alignvest Acquisition Corporation (AAC) announced on November 1, 2016 that it had entered into an arrangement agreement with Trilogy International Partners LLC. The agreement provides for an arrangement of AAC as a result of which AAC will acquire up to a 51% equity interest (and a 100% voting interest) in Trilogy. AAC intends to mail an information circular to shareholders by late December 2016 in connection with a meeting of shareholders anticipated to be held by late January 2017. Closing of the transaction is expected to occur shortly after the meeting of shareholders.

Acasta Enterprises Inc. (AEI) announced on November 10, 2016 that it had entered into agreements to acquire two private label consumer staples businesses and a commercial aviation finance advisory and asset management business. Completion of the transactions is expected to occur in January 2017.

Although the proposed transactions are not yet completed, they nevertheless give rise to some developments of potential interest to market participants:

- SPAC founders may have to reduce their "promote" or otherwise modify their initial investment to complete a qualifying acquisition
- a qualifying acquisition includes a sale of the SPAC, including one which results in the SPAC shareholders acquiring a minority interest in the ongoing business
- an arrangement of a SPAC may require only 50% approval of shareholders rather than the typical two-thirds approval for an arrangement

Reduction of the "promote"

The founders of a SPAC provide seed financing by acquiring units of the SPAC (shares and warrants) at the same price as the public investors in the IPO. The seed financing covers underwriting fees and legal and other expenses associated with the IPO and qualifying acquisition. Before its IPO, the founders of a SPAC acquire initial shareholdings for nominal consideration. These "founder shares" compensate the founders for the risk they have assumed with their seed capital, for their efforts in organizing the SPAC and for their ability to source and execute a successful qualifying acquisition. If certain share trading price thresholds are not achieved over time, 25% of these shares are subject to forfeiture for a period following completion of a qualifying acquisition.

In each of the IAC and DAC proposed transactions, the founders agreed to reduce the value accretion to be realized from their founders' shares on completion of the qualifying acquisition. In the case of IAC, the founders agreed to reduce the value of their founders' shares by 80% and, in the case of DAC, the founders agreed to reduce the value of their founders' shares by 25%. The sponsor of AAC has agreed to invest an additional $21 million at the IPO price of $10 per share and, together with certain other founders, has agreed to a lock-up of a portion of its shares for a period following closing of the qualifying acquisition (in addition to the shares subject to forfeiture). The founders of AEI have increased the number of their founders' shares that are subject to forfeiture if certain share trading price thresholds are not achieved over time, have increased such share trading price thresholds from those originally established at the time of the IPO and have agreed to invest an additional $10 million at the IPO price of $10 per share.

Sale of the SPAC

As noted above, each of the proposed IAC and DAC transactions was structured as an arrangement under corporate law, the steps of which included the acquisition of the shares of the SPAC. While it may be counter-intuitive that a qualifying acquisition could include a

sale of the SPAC, the acceptance by the TSX of this structure as a qualifying acquisition was likely based on the argument that the transaction is, in effect, a "merger" of the SPAC and the acquiror, since a merger is specifically contemplated as a potential qualifying acquisition in a SPAC prospectus.

It should also be noted that the IAC transaction contemplated the SPAC shareholders effectively acquiring only a minority interest in the ongoing business.

Voting threshold for SPAC arrangements

An interesting aspect of the proposed DAC transaction and the proposed AAC transaction is that each arrangement agreement contemplates that the shareholder approval threshold for the SPAC will be a majority (over 50%) of the votes cast in respect of the shareholders' resolution approving the arrangement. Typically, the approval threshold for shareholders of a corporation that is being arranged is two-thirds (or greater in some jurisdictions) of the votes cast in respect of the shareholders' resolution. Under applicable corporate law, this threshold is established by order of the court, but in practice, it has consistently been established by the court as the same threshold as applies to other "fundamental changes" under applicable corporate law such as amendments of articles, amalgamations and reorganizations.

Each of DAC and AAC is incorporated under the *Business Corporations Act*(Ontario) (OBCA). The OBCA provides that subject to any interim order of the court, where an arrangement is approved by shareholders by special resolution (i.e., by two-thirds of the votes cast) the corporation may apply to the court for approval of the arrangement. Clearly, the court has discretion to order a different shareholder approval threshold, but the presumption is that the threshold will be two-thirds. This presumption is further evidenced by the section of the OBCA that provides for the making of the interim order. It states that the court may make any interim order it considers appropriate, including an order that an arrangement must be approved by a specified majority that is greater than two-thirds of the votes cast at the meeting of shareholders.

The interim order of the court for the arrangement of DAC provides for an approval threshold of a simple majority. Counsel for DAC noted in its materials filed with the court that a simple majority approval threshold is consistent with the requirements of the TSX applicable to a SPAC's qualifying acquisition. Counsel also noted that the voting requirements in the interim order do not mean that the court has "set" or "established" the appropriate voting threshold which can be addressed at the court hearing to be held following the meeting of shareholders at which the court will be asked to approve the arrangement as fair and reasonable. Notably, at the time of this fairness hearing, the actual level of approval of shareholders will be known.

We believe that an argument that may be compelling to the court in seeking to establish a 50% shareholder approval threshold for the arrangement of a SPAC as opposed to the typical arrangement shareholder approval threshold of two-thirds is that, in the case of a SPAC, any shareholder of the SPAC (whether it votes in favour of or against the arrangement or does not vote) is entitled to require the SPAC to redeem its shares for its pro rata share of the escrowed cash of the SPAC. Accordingly, unlike a typical arrangement in which a shareholder would be required either to sell its securities in the market (which may not reflect fair value) or to dissent and pursue potentially costly litigation to achieve a "fair value" determination by the court in order to exit its investment, a SPAC shareholder can easily "get its money back" if it does not wish to remain invested.

It will be interesting to see the arguments that DAC and AAC make in support of the

suggested voting threshold in the proposed transactions and whether they find favour with the court.

We also expect there will be further developments in practice as the existing SPACs – and possibly new ones – move to complete their qualifying acquisitions. Market participants will be watching as the fate of the SPAC structure may hang in the balance.