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How SPAC Sponsors and De-SPACed Companies Can Protect Themselves as Valuations Plunge

The SPAC boom has turned into a bust, as many de-SPACed companies face cash constraints and even bankruptcy. This could invite scrutiny and disputes from shareholders, creditors or regulators against the companies and their sponsors. We explain how sponsors can prepare for the incoming legal and reputational troubles.

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SPACs saw a boom in 2020 and 2021, but many de-SPACed companies are now facing cash constraints and even bankruptcy. As these post-merger companies struggle to stay afloat, they and their sponsors should prepare to be best positioned should shareholders, creditors, or government regulators raise red flags over their conduct.

Anticipate sponsor scrutiny. The last year has seen a wave of shareholder suits against de-SPACed companies and their sponsors. These suits typically allege that mis-incentivized sponsors encouraged shareholders to approve an ill-advised merger, leading to significant post-merger losses. Delaware courts in particular have treated SPAC sponsors as controlling shareholders in some instances and allowed breach of fiduciary claims against them to survive motions to dismiss.

In this context, sponsors and de-SPACed companies should be preparing, with their advisors, a comprehensive legal strategy to respond to shareholder challenges. This includes the types of defensive tactics used in traditional mergers and acquisitions, such as hiring independent directors, ensuring fulsome disclosures to investors, and maintaining the independence of financial advisors who provide fairness opinions.

Mind the de-SPACed company's debt positions. SPACs have increasingly targeted companies with large, high-yield debt positions or relied on new debt financing to complete their de-SPAC transactions. These positions will be targeted aggressively in the event of further distress or a default, as some de-SPACed companies are already seeing. SPAC sponsors should plan proactively, including by assessing potential litigation risk from creditors seeking to enforce their positions.

Seize the narrative. If the sponsor does not take control of the narrative from the outset of a contentious litigation, impending bankruptcy, or enforcement action, its adversary will likely do so instead. Even in the absence of an immediate threat, it is still critical to develop a factual counter-narrative regarding the appropriateness of the transaction and all actions taken. This evidence can be deployed affirmatively, as appropriate, to strengthen the sponsor's position.

As the SPAC market continues to cool and de-SPACed companies see their valuations plunging, sponsors and their advisors should develop, with competent advisors, a plan which anticipates potential legal action as well as the financial and reputational consequences of negative press. Preparing for a litany of potential worst-case scenarios can save millions of dollars in the long run.

About Kobre & Kim

Kobre & Kim is a global law firm that focuses on cross-border disputes and investigations, often involving fraud and misconduct. Our team:

- Represents major corporations, investment funds and portfolio companies to litigate high-stakes trials and other commercial disputes adverse to major financial institutions and other market constituents.
- Acts in a variety of high-stakes creditor disputes, high-value M&A and corporate governance disputes, independent investigations on behalf of corporate boards, and in disputes involving equity and fixed income securities and complex derivatives.
- Offers deep experience coordinating strategies across jurisdictions, often involving clients, assets and adversaries in the PRC and other Asian countries, with lawyers admitted across the U.S., Asia, UK, EMEA, Latin America and key offshore financial centers.