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Spotify's Direct Listing Thrust 1 Firm Into April Spotlight

By **Tom Zanki**

Law360 (May 1, 2018, 8:23 PM EDT) -- Twelve operating companies went public in April and generated more than $3.3 billion in proceeds, but the month's standout deal was an unusual and potentially precedent-setting direct listing by streaming giant Spotify, advised by Latham & Watkins LLP, that raised no money.

Spotify's unorthodox public debut, in which the company did not issue new shares but instead listed its existing shares and allowed them to begin trading on the New York Stock Exchange, was unusual largely because the company did not hire underwriters to help it raise capital.

The novel approach limited the role of bankers, but the legal work that went into preparing Spotify's direct listing was extensive, according to the deals team at Latham & Watkins. Partners Marc Jaffe and Greg Rodgers said the firm began working on the transaction in May 2017, 11 months before Spotify's April 3 debut.

Latham lawyers said they devoted considerable time last year consulting with U.S. Securities and Exchange Commission staff, figuring out how to structure Spotify's filing and secure the agency's blessing. The process involved helping Spotify craft thorough disclosures and working with the company's financial advisers and NYSE in a way that would set the stage for a smooth debut.

"Because of the novel nature of the direct listing structure, the SEC and the Spotify deal team were focused on maximizing the likelihood of an orderly opening of trading in the stock," Jaffe said. "We didn't want to get to the opening of trading and have the stock experience wild movements in stock price, though we of course included disclosure of the risk that might occur despite our best efforts."

The potential for volatility was a big concern with Spotify since it was departing from the traditional initial public offering path, which typically includes a "lockup period" negotiated with underwriters that withholds most shares from being traded right after the IPO. Lockups are intended to limit the potential for unpredictable trading in the first few months after a company's public debut, but most of Spotify's shares immediately entered public markets free of those restrictions.

In its first month as a public company, Spotify's stock hasn't shown the volatility that was feared. Shares closed at $164.88 on Tuesday, which is about $1 less than where it began trading on April 3 and well above the $132 opening reference price set by the NYSE.

Looking back, Latham lawyers said Spotify's timeline wasn't much different from a standard IPO after the initial preparation was hammered out. Spotify filed confidentially with the SEC in December and made its plans public on Feb. 28, about five weeks before its market debut.

If another company chooses a direct listing approach, Jaffe and Rodgers said they expect the timetable won't be as long from start to finish now that there is a precedent.

"We would imagine the next similar direct listing could be accomplished on a much shorter time frame, all else being equal," Jaffe said.

As to whether more companies will pursue a direct listing, that possibility is likely limited to a few large private companies that are capitalized well enough that they don't urgently need new money and have enough name recognition that they can skip the usual pre-IPO marketing.

Spotify, which said it wanted to go public mostly to provide liquidity for its existing shareholders, may fit that mold — but lawyers say the vast bulk of potential public companies don't.

"Our experience shows the direct listing structure is a viable option," Rodgers said. "However, it's certainly not for everybody."

Spotify also went public during a receptive environment for technology IPOs, which generated more listings in April than any other sector, followed by life sciences. Latham, Cooley LLP, Davis Polk & Wardwell LLP, Fenwick & West LLP and Wilson Sonsini Goodrich & Rosati PC all advised on multiple listings in April, when including representation of issuers and underwriters.

The technology debuts fared especially well. Apart from Spotify, six technology companies went public through conventional IPOs in April and, through Tuesday, all their shares were trading up by double-digit percentages compared with their initial prices.

Capital markets lawyers advising technology issuers expect more deals to follow. For the past few years, companies in the technology sector have been slow to go public, opting instead to raise money privately, but that dynamic may be shifting again in favor of public markets.

"We are seeing lots of companies getting ready to go out," said Davis Polk partner Sarah Solum, whose firm also advised Spotify's financial advisers. "From what I am hearing, there is a lot of money that still wants to be put to work in the tech sector."

Electronic signature company DocuSign Inc. completed the largest traditional IPO among venture-backed startups, raising $629 million. The deal priced last week at $29 per share, above the range of $26 to $28 that was projected by DocuSign, which was represented by Cooley.

Zuora Inc. and Smartsheet Inc., two venture-backed software startups advised by Fenwick & West, raised $177 million and $175 million, respectively, in April. Both priced above their ranges and saw their shares rally after their debut.

At the higher end of the fundraising scale, Dell Technologies Inc. spinoff Pivotal Software Inc. raised $638.3 million after selling 42.6 million shares at $15 each. The share total for Pivotal, represented by Davis Polk, includes the underwriters' over-allotment option.

Payroll software firm Ceridian HCM Holding Inc. also raised $531.3 million in one of the month's largest deals. Private equity-backed Ceridian, represented by Weil Gotshal & Manges LLP, sold 24.15 million shares at $22 each, an amount that includes the underwriters' over-allotment option.

Few industries outside of technology and life sciences went public in April, though manufacturer GrafTech International Ltd. was among the exceptions. GrafTech, a maker of graphite electrodes used in steel production advised by Cleary Gottlieb Steen & Hamilton LLP, raised 38.1 million shares at $15 each. The GrafTech deal priced below its original range of $21 to 24.

In addition, insurance and banking companies went public with IPOs that raised less than $100 million each. Goosehead Insurance Inc., represented by Davis Polk, raised $85 million in a deal that priced below its projected range, while Level One Bancorp, represented by Barack Ferrazzano Kirschbaum & Nagelberg LLP, raised $34 million in an upsized deal.

Apart from operating companies, one blank check issuer went public in April. Pure Acquisition Inc. raised $414 million after selling 41.4 million units at $10 each. Fort Worth, Texas-based Pure Acquisition, represented by Thompson & Knight LLP, plans to acquire an energy company.

April IPO Recap

Twelve operating companies plus one blank check company went public in April, raising more than $3.7 billion in initial public offering proceeds. Here is a breakdown of the deals and the firms that advised them.

Issuer	Industry	Issuer Counsel	Underwriter Counsel	Total
Spotify Technology SA	Media, technology	Latham	--	N/A*
Pivotal Software Inc.	Technology	Davis Polk	Fenwick & West	$638M
DocuSign Inc.	Technology	Cooley	Davis Polk	$629M
GrafTech International Ltd.	Manufacturing	Cleary	Cravath	$572M
Ceridian HCM Holding Inc.	Technology	Weil	Latham	$531M
Pure Acquisition Corp.	Blank Check	Thompson & Knight	Greenberg Traurig	$414M
MorphoSys AG	Life Sciences	Skadden	Latham	$239M
Zuora Inc.	Technology	Fenwick & West	Wilson Sonsini	$177M

Issuer	Industry	Issuer Counsel	Underwriter Counsel	Total
Smartsheet Inc.	Technology	Fenwick & West	Wilson Sonsini	$175M
nLight Inc.	Technology	Wilson Sonsini	O'Melveny & Myers	$110M
Surface Oncology Inc.	Life Sciences	Goodwin Procter	Cooley	$108M
Goosehead Insurance Inc.	Insurance	Davis Polk	Simpson Thacher	$85M
Level One Bancorp	Banking	Barack Ferrazzano	Silver Freedman	$39M

**Spotify listed its existing shares directly and did not raise any new proceeds. The company also did not hire underwriters in a traditional sense, though Davis Polk & Wardwell LLP represented financial advisers who assisted with the direct listing.* Source: Nasdaq.com and Renaissance Capital Created with Datawrapper

--Editing by Philip Shea and Alanna Weissman.