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# SPACs IN EUROPE

Special purpose acquisition companies (SPACs) have gained increasing attention over the past year, largely due to the recent surge of SPAC offerings in the United States. While SPACs have been a less common means of capital markets financing and listing in Europe, a number of recent and anticipated offerings by SPACs indicate that this may be changing. This client briefing provides a high-level overview of common SPAC features, key considerations for SPACs in Europe as well as issues raised in offerings by SPACs to qualified institutional buyers in the United States.

**Key issues**

- In Europe, the specific characteristics of SPACs and similar structures can vary depending on the corporate law of the relevant jurisdiction, stock exchange rules as well as marketing considerations.
- Sponsors should be prepared to discuss with regulators how the SPAC's prospectus will provide investors with sufficient information to make an investment decision, notwithstanding the lack of identified target businesses or assets.
- Sponsors should approach the competent regulator early in the process to ensure that they would not view the SPAC as an alternative investment fund governed by the EU Alternative Investment Fund Managers Directive.
- Given the potential for differing views among regulators on multiple issues affecting SPACs, one aspect to watch going forward will be whether regulators on the European or national levels will undertake any initiatives to address the SPAC trend.

## WHAT IS A SPAC?

SPACs are companies without their own business operations that offer units for sale to investors and then use the proceeds of the offering to acquire businesses or assets that have yet to be identified. The units typically comprise shares as well as fractions of warrants that entitle their holders to acquire additional shares at a premium to the IPO offer price. Because the SPAC does not have its own business at the time of the offering, investors are effectively making an investment in the SPAC's sponsors and their ability to complete an acquisition of a suitable target. For this reason, the sponsors and management teams typically have established a successful track record in a particular industry.

Because upon completion of an acquisition, SPACs effectively take the acquired (usually privately held) businesses public, they are considered an alternative to the traditional IPO, which may involve a more time-intensive listing and disclosure process.

## TYPICAL SPAC FEATURES

Many of the characteristics common to SPACs have their origin in Rule 419 under the U.S. Securities Act, which imposes certain requirements on public offerings of so-called "blank check companies" in the United States. In Europe, the specific characteristics of SPACs and similar structures can vary depending on the corporate law of the relevant jurisdiction, stock exchange rules as well as marketing considerations. SPACs as they are known in the United States typically have the following features:

### *Unidentified Target*

The defining characteristic of a SPAC is that, at the time of IPO, it has not identified target businesses or assets to be acquired. If the SPAC were to have already identified a probable target for acquisition, then the SPAC would likely be required to include detailed disclosure on the target in its prospectus, thereby eliminating a key benefit of the SPAC structure. Instead, most SPACs state that they will seek to acquire a target in a particular geographic market and industry, while the specific target remains unknown.

***Acquisition Deadline***

Following the offering, the SPAC usually has a certain period of time (typically two years) within which to acquire businesses or assets, which the SPAC's governing documents may permit to be extended under certain circumstances. The SPAC usually commits to returning the proceeds of the offering to its shareholders if it fails to complete an acquisition within the specified time.

***Proceeds Held in Escrow***

SPACs typically provide that the proceeds of the offering will be held in an escrow account. The proceeds in the escrow account may be used to fund an acquisition that is approved by the SPAC's shareholders, to redeem the shares of any shareholders who choose to exercise redemption rights, or to return funds to the shareholders if no acquisition is completed and the SPAC is liquidated.

***Shareholder Approval of Acquisitions***

Once the SPAC has signed an agreement to acquire target businesses or assets, the SPAC will put the acquisition to a vote by the shareholders. SPACs usually require a majority of the votes cast to vote in favor of an acquisition, unless a greater number of votes is required for a merger or other type of business combination under the corporate law of the relevant jurisdiction. Some SPACs have required higher thresholds for shareholder approval, such as 70%. In advance of the shareholder meeting, the SPAC will prepare detailed disclosure on the target's business and financial information on which the shareholders can base their decision, in accordance with the requirements of the SPAC's jurisdiction.

***Redemption Right***

SPACs usually provide their shareholders with the right to have their shares redeemed for cash if they choose not to remain invested in the company upon the completion of an acquisition. While some SPACs only allow shareholders who vote against the proposed acquisition to exercise their redemption rights, others have no such requirement, instead allowing shareholders to redeem their shares regardless of whether and how they vote on the acquisition.

***Units Comprising Shares and Warrants***

The units offered in a SPAC's IPO comprise shares as well as fractions of warrants that entitle their holders to acquire additional shares at a premium to the IPO offer price. Generally, the shares and warrants of SPACs in the United States initially trade together as units and begin trading separately on a later date while, on European exchanges, the shares and warrants typically trade separately from the first day of trading.

The warrants provide an incentive to invest in the SPAC's IPO if the SPAC completes an acquisition that is viewed positively by the market and results in the market price of its shares rising above the warrants' strike price. In Europe, if the units are offered at, for example, a price of EUR 10 per unit, the warrants can typically be exercised at a price of EUR 11.50 per share. The warrants usually become exercisable 30 days following an acquisition. If the market price of the shares rises above a specified price for a certain period, the SPAC has the option to redeem the warrants for a nominal price. Unless exercised or redeemed, the warrants expire after a specified period, such as five years following the acquisition.

## SPAC DISCLOSURE

Due to a SPAC's lack of business operations at the time of prospectus approval, the prospectus disclosure is brief compared to that of a traditional IPO. The disclosure usually focuses on the management team's track record in a particular industry, the industry and geographic markets in which they will seek to acquire businesses or assets, as well as their strategy for sourcing potential acquisitions. The section describing the risk factors usually discloses risks related to the issuer's lack of operating history, potential loss of members of the management team, inability to complete an acquisition, as well as any general risks that may be associated with an industry in which the SPAC intends to acquire businesses or assets.

Since a SPAC is usually incorporated shortly before its IPO, the financial disclosure contained in a SPAC's prospectus is usually less important than in a traditional IPO and included only to the extent necessary to satisfy minimum regulatory requirements, typically including financial statements covering the period from the date of the SPAC's incorporation until the end of the last reporting period.

## KEY LEGAL CONSIDERATIONS FOR SPACS IN EUROPE

While originally a U.S. phenomenon, interest in the SPAC structure has been growing in Europe. The extent to which the SPAC structure can be replicated will depend on several factors, such as the views of the national regulator that is competent to approve the SPAC's prospectus (which will depend on the SPAC's jurisdiction of incorporation), the flexibility of that jurisdiction's corporate law in allowing typical SPAC features to be implemented, as well as the listing rules of the stock exchange on which the SPAC will be listed.

***Competent Authority for Prospectus Approval***

A question SPAC sponsors must consider early in the process is which jurisdiction they will incorporate the listing vehicle in, which will determine the national regulator that is competent to approve the issuer's prospectus. Regulators in France, Italy, Luxembourg, the Netherlands and the United Kingdom have recently approved prospectuses for SPACs. Sponsors should be prepared to discuss with regulators how the SPAC's prospectus will provide investors with sufficient information to make an investment decision, notwithstanding the lack of identified target businesses or assets.

***Corporate Form***

In choosing the jurisdiction and legal form for incorporation of the SPAC, sponsors must consider the extent to which typical SPAC features can be implemented under a jurisdiction's corporate law.

For example, some legal forms such as the German stock corporation restrict the management's ability to return capital to shareholders and impose lengthy processes for liquidation to protect creditors. Such restrictions can hinder the SPAC's ability to return the IPO proceeds to shareholders if an acquisition is not approved by the shareholders or otherwise not completed within the specified time. The European company (SE) incorporated in Luxembourg and the Dutch private company with limited liability (B.V.) have been common choices for recent European SPACs.

### *Alternative Investment Fund Managers Directive*

The Alternative Investment Fund Managers Directive and national legislation implementing it govern alternative investment fund managers based in the European Union and non-EU countries within the European Economic Area and any fund marketing activities within the EU and the EEA. The directive prohibits the management of an alternative investment fund ("AIF") or marketing shares or units in an AIF without having the relevant management or marketing authorization. Similar regulation exists for the United Kingdom. To not qualify as an AIF, SPACs can be structured to fall within the exemptions provided for operating companies outside the financial sector or holding companies. Due to the lack of authoritative guidance in relation to SPACs and the potential for differing views among regulators, however, sponsors should approach the competent regulator early in the process to ensure that they would not view the SPAC as an AIF.

## CONSIDERATIONS FOR RULE 144A OFFERINGS

### *Investment Company Act*

If the SPAC will offer units in an offering to qualified institutional buyers in the United States under Rule 144A, then sponsors should also be aware of considerations under the U.S. Investment Company Act of 1940. The Investment Company Act governs the activities of companies that invest in securities, such as mutual funds and other collective investment vehicles.

To avoid qualifying as an investment company, SPACs in the United States typically provide that funds held in escrow prior to an acquisition will be invested in short-term U.S. government securities or held as cash, as other investments could be considered investment securities. In Rule 144A offerings, SPACs usually rely on the exemption provided by Section 3(c)(7) of the Investment Company Act by restricting sales of their units to qualified institutional buyers that are also qualified purchasers under the Investment Company Act. In addition, SPACs usually acquire a controlling interest in their targets to avoid having their shareholdings qualify as investment securities.

### *Volcker Rule*

SPACs that rely exclusively on the Section 3(c)(7) exemption mentioned above to avoid being an "investment company" for purposes of the Investment Company Act may be considered a "covered fund" under the Volcker Rule of the Dodd-Frank Act. Banking entities subject to the Volcker Rule and their affiliates would be restricted from acquiring ownership interests in a SPAC that is a covered fund, which could adversely affect the demand for securities offered by the SPAC and may reduce secondary market liquidity for these securities.

## CONCLUSION

It remains to be seen whether recent and anticipated SPAC offerings in Europe are a sign that Europe will experience a surge in SPAC offerings as seen over the past year in the United States. Given the potential for differing views among regulators on multiple issues affecting SPACs, one aspect to watch going forward will be whether regulators on the European or national levels will undertake any initiatives to address the SPAC trend.

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