An attractive alternative to raising capital: Acquisition IPOs are SPAC

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SPACs (Special Purpose Acquisition Companies) are trending and not only in the North American market where these vehicles have been popular for a number of years. They are now gaining interest from investors globally and particularly in the UK.

Earlier this year and during the initial stages of the pandemic we experienced a resurgence of interest in Jersey cash box structures as a quick means of raising capital for UK listed companies. With private equity and venture capitalist investors looking at acquisition targets and searching for yield within an opportunistic environment, SPACs have become an appealing and increasingly popular alternative to the traditional IPO process. These vehicles also seem to mirror a similar cycle to that of the cash box structures, in that their popularity seems to have increased as a result of market volatility and a demand for cash liquidity caused by the recent pandemic, similar to the period following the financial crisis in 2008.

What is a SPAC?

It's a newly incorporated company founded by one or more sponsors, with the single objective of making one or more target "acquisitions". The funds are raised through the IPO process and investors will "buy-in" to the track record and experience of its founders/sponsors, often being high profile wealthy entrepreneurs or private equity partners.

The special purpose vehicle will be listed on a chosen exchange and investors and the founders/ sponsors receive shares or warrants (long-term options giving a right but not an obligation) to purchase shares at a set price within a specified period) in the vehicle, with the founders/sponsors typically receiving 10-20%.

The investment strategy for the acquisition published in its listing document would usually be expected to be completed by the founders/ sponsors within approximately 18-24 months (depending on the rules of the exchange), hence these vehicles often being referred to as "cash shells" or "blank cheque vehicles". Many SPACs also have a minimum transaction size requirement of approximately 80% of available funds.

Interestingly, whilst the SPAC can acquire assets through a simple purchase of another entity, there have been a variety of corporate techniques used to make these "acquisitions", including takeovers, mergers with a target and retaining rights in the surviving entity, raising additional funding, being "purchased" by a target (with equity in return) or a reverse takeover where a private (non-listed) company is acquired by the SPAC and then merged with it. As such, they can be seen as a new way of doing an M&A deal and having a suitably wide definition of the permitted "business combinations" for the acquisition provides useful flexibility.

Key features of the SPAC process

The features will be dictated somewhat by the market and exchange which the vehicle is listed, although there are some fundamental points which will need to be considered and potentially supported by a 3rd party. These are:

- **Incorporation** – Incorporation of the company in the jurisdiction of choice and arranging the key corporate requirements including company secretary, registered office, administration, compliance and accounting.
- **IPO and holding funds** – Compliance with listing requirements, listing application/approval and management of the cash received (which would be typically placed into an interest bearing escrow/treasury/trust account) and cashflow management to deliver returns which can cover working capital expenses incurred between IPO and acquisition.
- **Operation and management of the SPAC** – Given the nature of these vehicles, the establishment and running costs associated with supporting SPACs should generally be lower than other more active vehicles, such as investment funds. They will however continue to require governance, compliance, accounting and listing rules monitoring support. It is important to ensure you have visibility and transparency on costs as this can be a distinguishing feature when deciding to outsource the corporate administration.
- **Acquisition / M&A** – Using IPO proceeds, debt and issuance of equity, the acquisition can be achieved in various ways (as outlined above). Co-ordination and project management by an administrator present in the various jurisdictions can help manage associated costs and work to be undertaken for this corporate event. Depending on the exchange, there may be a variety of shareholder approvals, listing compliance approvals and prospectus issues to be considered.
- **Liquidation / wind up** – Liquidation may occur if the investment strategy is not executed within the required timeframe and monies will need to be returned to the investors.

Recent examples

High profile recent SPAC IPOs include Richard Branson's Virgin Galactic (merged and taken public by a SPAC which raised $800m) as well as his recent new business venture through VG Acquisition Corp. ($400m, Cayman Company). US healthcare company MultiPlan also went public in an $11bn merger with a SPAC, Churchill Capital Corp III, which raised $1.1bn in February 2020.

In terms of asset class, SPACs are well known for being weighted to technology and growth companies.

The NYSE exchange has reportedly seen 55 SPACs raising $22.5b as at early September this year. This compares to 59 SPAC IPOs collectively raising $13.6b in 2019.

Whilst the London Stock Exchange has not reached similar levels in terms of both volume and value, the trend is significantly upwards with a 30% increase in market value of SPAC IPOs in 2019, over 50 SPACs over the last 5 year and over $2bn raised since 2017.

Benefits of a SPAC and attraction to investors

Whether listing on the NYSE, Nasdaq, LSE, AIM, or TISE, all will be comparatively more flexible and lighter on regulation than a premium main market listing (which may not be available because of a lack of trading history). Some of the relaxations being provided by exchanges include:

- A simple and straightforward process for listing a SPAC
- Less time and cost when compared to the traditional IPO process with various road shows
- No requirement to appoint a financial adviser, sponsor or a Nomad (an AIM listed SPAC must have a Nomad)
- Low required minimum market capitalisation
- Potentially flexible application of corporate governance codes
- May not need to provide shareholders with pre-emption rights
- May not need shareholder approval for reverse takeovers or acquisitions
- May not be subject to any time limit to make its initial investments (or a fairly long timescale)
- Generally has greater flexibility around share dealings and related party transactions
- Low cost corporate administration to support the incorporated company during the IPO and acquisition process

Speculative investors will undoubtedly have their preferences on the type of exchange used, and this will be a key driver for the founders of the SPAC who may wish to attract certain types of investors. We have also seen geographical factors at play, such as the attraction of the UK markets for Asian investors and high-net worth entrepreneurs. SPACs are also attractive to hedge funds which can view the holding as a cash proxy and provide investors who can only invest in listed securities with exposure to private companies with illiquid securities.

A listed SPAC can be used to access a greater range of investors than are typically possible in private equity fund structures which are sometimes restricted to professional and institutional investors by law or regulation.

Is a SPAC a fund?

SPACs sometimes resemble investment funds in that they can have a collective pooling of capital, can be making multiple investments (therefore arguably risk spreading), allow discretion to the management team to make investments on their behalf and invest in similar types of assets as a private equity fund.

The costs associated with establishing a SPAC and its supporting structure are generally lower than those applicable to a fund. A SPAC does not require a fund management company to be established. This saves time and cost of set-up and compliance with regulations applicable to funds and managers.

It should also be noted that SPACs' investment policies and objectives are not (usually) intended to achieve a spread of risk for investors. The regulatory frameworks of certain jurisdictions and how they identify investment funds can impact on the proposed jurisdiction for certain multi-investment SPACs.

Why have an offshore SPAC?

There are a number of advantages to using an offshore SPAC, most notably:

- Reduced cost compared to other structuring options

- Ecosystem of experienced service providers and advisers
- Regulatory flexibility as regards SPACs, investment funds classification and capital raising but a robust regulatory environment
- Flexible companies laws in the Channel Islands and Caribbean adaptable to the rules of most exchanges, including regarding dividends, financial assistance, tax neutrality for global investors and for the variety of corporate acquisition techniques (such as takeover, merger etc).
- Established track record of their use for SPACs

Conclusion

Whilst investment in SPACs should always be considered carefully by investors due to the discretion provided to the sponsors/founders, they are proving to be a real source of market activity and an attractive proposition for experienced private equity experts looking to take advantage of market conditions and deliver quick returns against that next target unicorn.

For more information about we can support please contact Sam Sturrock (Group Partner) at sam.sturrock@collascrill.com or +44 (0)1534 601742 or Shervin Binesh (Director, Corporate Services) at shervin.binesh@sannegroup.com or +44 1534 710206 in relation to the establishment of an offshore SPAC.

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