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The UK Reforms That Add Investor Allure To SPACs

By **Marcus Young and William Morris** (September 20, 2021, 3:51 PM EDT)

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Special purpose acquisition companies have been a hot topic in the past year, with international exchanges clamoring to attract SPACs and land lucrative listings.

Often known as blank check companies, SPACs are shells that raise money in initial public offerings and then acquire firms in de-SPAC transactions. While SPACs are not new, their popularity has rocketed in the past two years, with SPAC IPO activity and deal volumes increasing exponentially in 2020 and the first quarter of this year, with most activity occurring in the U.S.

Although second-quarter SPAC activity showed a marked quarter-to-quarter slowdown following new U.S. Securities and Exchange Commission guidance on accounting for share warrants, significant appetite appears to remain in the market for the SPAC structure.

Understandably, regulators and financial authorities have been looking at reforms to entice more SPACs to their stock exchanges. And the Financial Conduct Authority is the latest such body do so.

On July 27, the FCA implemented changes to the rules for SPACs intending to list on the main market of the London Stock Exchange. The new rules implement a recommendation of Jonathan Hill, the European Union's former financial services commissioner, and also follow an April FCA consultation paper on the same topic.

The U.K. has been slow to benefit from the opportunities presented by the popularity of the SPAC structure. This is at least in part because of the general presumption for a SPAC to have its listing suspended upon the identification of a potential acquisition target, on the basis that the suspension would prevent the creation of disorderly markets arising from a lack of information being publicly available.

This automatic suspension was seen by investors as undesirable as it would prevent the sale of their shares for undetermined periods. The new rules have removed this requirement, subject to satisfaction of certain conditions.

The Regulatory Differences

Specifically, the new rules remove the general presumption that a SPAC will have its listing suspended when it announces an acquisition target, provided that the SPAC has the following structural features:

- A minimum size threshold of £100 million ($136.8 million) raised when a SPAC's shares are initially listed. Following market feedback, this threshold was reduced from the £200 million suggested in the FCA's consultation proposal.

- Monies raised on IPO must be ring-fenced by the SPAC to be used only in the following circumstances:

    - As consideration for a reverse takeover;

    - To redeem or repurchase its own shares;

    - To return to shareholders in the event a reverse takeover has not taken place within a specified timeframe; or

    - To return to shareholders in the event of a winding-up of the SPAC.

- The SPAC is permitted to exclude a specified amount from the ring-fencing requirement for its running costs, provided this amount is disclosed in its prospectus.

- There is a set time limit to find and acquire a target within two years of admission to listing, which may be extended by 12 months, subject to shareholder approval.

- In certain limited circumstances, this time limit may also be extended by six months without shareholder approval; for example, when the SPAC shareholders have already approved the proposed acquisition.

- Board approval is required for any proposed acquisition, excluding — from the board discussion and vote — any board member who is, or has an associate who is, a director of the target or its subsidiaries, or has a conflict of interest in relation to the target or its subsidiaries.

- In the event of such a conflict, the board will need to publish a fair and reasonable statement that reflects advice from an appropriately qualified and independent adviser.

- Shareholder approval is required for any proposed acquisition, with SPAC founders, sponsors and directors to be excluded from voting.

- A redemption option allows investors to exit their shareholding before any acquisition is completed.

- Investors will be provided sufficient disclosure on key terms and risks from the SPAC IPO through to the announcement and conclusion of any acquisition. This requirement will work in tandem with existing disclosure requirements under the Prospectus Regulation and Market Abuse Regulation, with additional clarity on specific disclosures to be made at the time of a de-SPAC transaction, including all material details that the SPAC is — or ought reasonably to be — aware of about the target and the proposed deal.

The SPAC must provide confirmation in writing to the FCA that these conditions have been met and will continue to be met until after completion of the de-SPAC.

In addition, the FCA has stated that it will confirm upfront whether a proposed SPAC satisfies the new rules on avoiding the suspension presumption, as part of the eligibility and prospectus vetting process.

In the consultation paper, the FCA had proposed that SPACs seeking to avoid a suspension would need to contact the FCA at the point of de-SPAC to determine the SPAC's eligibility to avoid the suspension presumption.

This clarification is to be welcomed, as otherwise significant time and money could be expended on a transaction which the FCA ultimately determine is not eligible.

What the Rules Mean for the U.K. Financial Markets

The FCA has stated that through the introduction of these measures, it aims to "make markets function well and promote market integrity and consumer protection by providing a more flexible approach for SPACs of a certain size that embed features that strengthen protections for investors and maintain the smooth operation of markets."

The removal of the suspension presumption removes a significant disincentive to list SPACs in London and should make it easier to market SPACs to prospective investors on IPO.

It is also encouraging to see the FCA heed the advice it received during consultation and reduce the minimum size threshold to £100 million from £200 million. Throughout its policy statement, the FCA has maintained that it will not be prescriptive with certain elements, in particular with respect to ongoing disclosure requirements where it has rejected the suggestion that it adopt a U.S.-style approach to disclosure through the life-cycle of the SPAC and de-SPAC.

Generally, the rules that a SPAC looking to list in London will have to comply with in order to avoid the suspension presumption are broadly similar in the main SPAC listing venues — i.e., the U.S., Amsterdam and Frankfurt — and this should help to level the playing field for the U.K.

There do, however, remain some key differences between the U.K. regime and those in the U.S. and Europe, namely:

- The sponsor and its directors will be precluded from voting on the de-SPAC transaction.
- The U.K. listing rules still mandate that the issuer will have to prepare a prospectus and apply for listing of the enlarged group in tandem with the de-SPAC transaction.
- The SPAC will have to announce how it has valued and assessed the SPAC, making specific reference to the selection criteria and procedure laid down in the prospectus published in connection with listing of the SPAC's shares.
- U.K. SPACs will not be permitted to list units. This differs from the approach in the U.S. exchanges and on Euronext, meaning that SPACs will only be able to offer ordinary shares and warrants. However, in its policy statement, the FCA has made it clear that it will keep this regulation under consideration given the use of units on other exchanges.

Effective as of Sept. 3, the Singapore Exchange has revised its listing rules by introducing new rules that enable SPACs to list on its main board. In order for a SPAC to achieve a Singapore Exchange listing it must have the following key features:

- The SPAC must hold a minimum market cap of 150 million Singapore dollars ($111 million).
- The de-SPAC transaction must take place within 24 months of IPO with an extension of up to 12 months subject to fulfillment of prescribed conditions.
- There must be a moratorium on sponsors' shares from IPO to de-SPAC, a six-month moratorium after de-SPAC and for applicable resulting issuers, a further six-month moratorium thereafter on 50% of shareholdings.
- Sponsors must subscribe to at least 2.5% to 3.5% — depending on the market capitalization of the SPAC — of the IPO shares, units or warrants.
- The de-SPAC will require approval of a majority of independent directors and a majority of shareholders.
- Warrants issued to shareholders must be detachable and the maximum dilution to shareholdings arising from the conversion of warrants issued at IPO is capped at 50%.
- All independent shareholders must be entitled to redemption rights.
- There must be a sponsor promotion limit of up to 20% of issued shares at IPO.

There are several similarities between this regime and the requirements under the U.K. listing rules to avoid the suspension presumption. The market capitalization requirement and the long stop date for the occurrence of the de-SPAC transaction are broadly the same, although Singapore will be more appealing to smaller SPACs due to the smaller market cap requirement.

The main difference between the requirements of the Singapore Exchange rules and the U.K. listing rules is that SPACs listing on the Singapore Exchange will be able to offer units, akin to the regime in the U.S. The FCA has also baked in more protections with respect to the capital raised from listing with the requirement to ring-fence these monies.

The FCA has stated that it will keep the new requirements for disapplication of the suspension presumption under review, and we may therefore see further changes in due course.

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