May 7, 2021

European SPACs – Following in America's Footsteps?

Jeffrey M Bronheim; Muriel Goldberg-Darmon; Bonnie J Roe; Daniel H Mathias

Introduction – what are SPACs?

A Special Purpose Acquisition Company, or '**SPAC,**' is a company created with cash only for the purpose of acquiring one or more businesses (the UK 'blank-check company' is very similar). SPACs are incorporated by a team of sponsors and initially raise capital through the public markets more quickly than a traditional IPO. Once capital has been raised, the sponsors seek to identify one or more private companies to purchase. The sponsors will generally target a specific industry or sector in which they have particular expertise. Once identified and a transaction is agreed, the SPAC will be combined with the target (this is known as a de-SPAC merger). In effect, this process is a reverse merger through which the private target becomes the resulting public company.

Typically, the sponsors will have two years to invest the funds raised by the SPAC, failing which they will be required to return the funds to investors and dissolve the company (some SPACs provide for a shareholder vote to extend their life if no target has been found). Although SPACs following this model have existed for over a decade, they have proliferated recently, particularly in the U.S., and with the involvement of several high-profile figures and celebrities as sponsors.

In this client alert, we will consider the U.S. SPAC regime (currently the most prominent venue for SPACs), as well as those European financial centers seeking potential growth in this market.

The U.S. SPAC Regime

While SPACs have existed as an investment and capital raising mechanism for many years, they have truly proliferated over the past few years in the U.S. In an era of low interest rates, investors have continued to seek new opportunities, with SPACs offering the opportunity to invest in an IPO on favorable terms or receive their money back if they do not like the proposed merger partner. By some estimates, more than $100 billion has been raised this year alone through SPACs – already more than in 2019 and 2020 combined.

U.S. SPACs are characterized by a number of key features which make them attractive mechanisms for conducting reverse mergers. Possibly the most attractive feature of U.S. SPACs for investors is that once the SPAC identifies a target, shareholder approval is required for any acquisition. This "approve or redeem" feature does not currently apply to UK SPACs on the Standard segment of the Official List (the most popular venue for listing UK SPACS). It adds a layer of protection and liquidity for investors by providing them with the option to withdraw their investment rather than participate in an unattractive acquisition. As part of this process, though, the SPAC will generally have to prepare and file an SEC-compliant proxy statement setting out the terms of the proposed merger in detail. Somewhat counterbalancing the obvious benefits to investors, this process can be a lengthy one, which may not please the target. Although many targets assume that a de-SPAC merger will streamline the process of going public (compared to a traditional IPO route), there are many regulatory hurdles. The target must provide compliant financial statements and other information concerning its business to the SPAC shareholders in connection with the merger and must file this information with the U.S. Securities and Exchange Commission (the "SEC"). The target must also be ready to comply with stock exchange listing requirements.

Once the SPAC shareholders have approved the merger, and all regulatory hurdles have been cleared, the merger concludes, and the target becomes public.

In response to the frenzied activity surrounding SPACs of late, the SEC has now taken a cautious approach and begun to scrutinize such transactions more carefully. In a recent announcement on April 12 2021, the SEC indicated that certain SPACs might have failed to properly account for the warrants given to the sponsors, on occasion listing them as equity instruments where they would more appropriately be classed as liabilities. As a result, some SPACs may have to restate their financial statements to reflect the quarterly variations in the value of their warrants – a potentially lengthy, technical process.

In addition, the SEC has released a statement regarding SPACs' potentially inflated earnings projections, noting that it will look to scrutinize these in greater detail going forward. Traditionally, a perceived advantage of SPACs has been the ability to release more optimistic earnings projections in relation to the nascent or pre-revenue companies which they acquire. On the other hand, the IPO process generally delivers more conservative estimates in light of potential legal liabilities. While there is no safe harbor for forward-looking information in the traditional IPO process, de-SPAC transactions have taken advantage of provisions that allow for the use of projections in connection with a merger. Whether these disclosures should be eligible for safe harbor protection from liability, as they would in connection with a normal merger, is now being questioned by the SEC.

While the SEC's recent guidance may cause U.S. SPACs to pause to reflect on the practical impact of regulatory intervention, the European markets are seeking to explore ways to reform their existing regulatory treatment of SPAC structures to encourage them.

The UK SPAC Regime

On March 3, 2021, a review of the UK listing regulations led by Lord Johnathan Hill, former EU financial stability chief, was unveiled by the UK Government. The review set out to propose regulatory changes that would attract promising companies to list in London in a bid to protect the city's reputation as a leading financial hub post-Brexit.

According to Lord Hill's UK listing regulations review (see below), only four SPACs were listed in the UK in 2020, raising an aggregate total of £300 million (a tiny fraction compared to the U.S.). This paucity of SPAC activity can partly be explained by the fact that London's FCA rules and regime do not require investors to have the right to redeem their shares if they do not approve of the target acquisition, although sponsors can choose to include such right.

Another characteristic of UK-listed SPACs is that the transaction is deemed a reverse takeover, and trading in the SPAC's shares are suspended from when the merger is announced until a prospectus is published (with no prescribed deadline in force). This, in effect, means that SPAC investors who are not supportive of the transaction are potentially locked-in for an uncertain period of time.

Lord Hill's Review

Lord Hill's review outlined a number of key proposals for amendments to the UK listing regime in an effort to bolster London's stock market's attractiveness for SPACs. These include reducing free float requirements from 25% to 15% to avoid diluting early backers, and permitting dual-class share structures on the FCA's Premium Listing Segment (subject to limitations) to afford greater control to sponsors.

The review also proposed additional rule changes to make UK SPACs more attractive. These changes include:

- Removing the presumption of suspension of trading in a SPAC's shares following the identification of an acquisition target;
- If necessary, to determine the size of SPAC below which the suspension presumption may remain in force, in order to safeguard market integrity;
- Amending the liability regime applicable to issuers and facilitating the inclusion of forward-looking information in prospectuses;
- Introducing a right for investors to vote on proposed acquisitions prior to their completion or to redeem their investment.

The first step was unveiled on April 30 2021, as the FCA announced that it had launched its consultation on proposed changes to its Listing Rules for certain SPACs. The announcement, which confirmed that there are circa 33 SPACs listed in the UK, of which 13 currently have their listing suspended, included a number of proposals on which it is seeking feedback, including:

- Removing the requirement for SPAC listings to be suspended when the SPAC identifies an acquisition target;
- Setting the bar for which SPACs can avoid suspension on the identification of a target at £200m raised in the initial IPO;
- Ensuring monies raised from public shareholders are ring-fenced to either fund an acquisition or be returned to shareholders, less any amounts agreed to be used for the running costs of the SPAC;
- A 'redemption' option allowing investors to exit a SPAC prior to any acquisition being completed;
- A time limit on a SPAC's operating period if no acquisition is completed; and
- Tightened disclosure rules.

These measures, it is hoped in some quarters, will be approved by the FCA after its consultation on relevant changes to its rules over the coming summer and adopted formally by the end of this year at the latest. The speed of the FCA's review will be determinative of London's standing when it comes to SPAC listings.

The French SPAC Regime

Although prominent business figures in France such as Tidjane Thiam and Bernard Arnault have been involved in SPACs, France has, so far, (similarly to the UK), lagged as a jurisdiction of choice for SPAC listings. For instance, Arnault listed his SPAC vehicle in Amsterdam – which has so far emerged as the European venue of choice for SPACs – while Thiam's was set up in New York. Indeed, only two SPACs were listed in France: Mediawan in 2016 and 2MX Organic in 2020, whose main sponsors were, in both cases, Xavier Niel and Matthieu Pigasse. The two SPACS were listed on the professional compartment of the regulated market Euronext Paris, dedicated to qualified investors.

Nevertheless, France is looking to capitalize on the upward trend of SPAC listings and investment. The Autorité des Marchés Financiers (the "AMF"), the French financial markets authority, noted in an April 15, 2021 press statement that it had observed a significant increase in the number of SPACs preparing their listings on the Paris stock exchange – Euronext Paris – so far this year. The statement outlined a number of factors that make Paris an attractive venue for listing SPACs. By and large, this boils down to having a similar regulatory regime to the U.S. Among the regulatory characteristics vaunted by the AMF are the following:

- the preference share system makes it possible to create shares with specific rights and to make a distinction, within the framework of a SPAC, between the shares subscribed by sponsors and those offered to investors;

- redeemable preference shares can be offered to investors, which allows them, under certain conditions, to have their shares redeemed by the SPAC if they do not wish to remain shareholders in the company once merger (or purchase of the target) has been completed;

- warrants allow investors to acquire shares at a predetermined price in the future and thus benefit from the company's prospective success should the company's value increase after the merger or target purchase. The option to issue warrants also affords SPACs the flexibility to raise any additional funds necessitated for a merger; and

- the AMF will carefully scrutinize SPAC prospectuses pre-listing – in English if the issuer so wishes – applying its practical experience to the process.

France will be hoping that going forward, its sponsor-friendly yet investor-safe regime will convince investors to support SPACs on Euronext Paris, and promising companies will, in turn, opt to merge with, or be purchased by, the growing number of French SPACs.

Other financial centers in Europe

A number of further European financial hubs, such as Frankfurt, are beginning to attract SPAC formations and investment. However, Amsterdam, in particular, has seen a number of SPAC listings over the past couple of years, including a vehicle launched by Bernard Arnault (as mentioned above). Sponsors have likely been attracted by its capital market-friendly reputation and investor-friendly listing rules, which, similar to those in the U.S., allow investors to opt-out of their investment either before or after a target acquisition has been announced.

Conclusion

While commentators are split on the likely long-term impact of the recent SEC commentary and guidance, the U.S. is currently experiencing a reduction in SPAC listings. Nevertheless, a number of European financial centers now appear in a footrace amongst themselves to tailor and/or market their regulatory regimes to potential sponsors, investors and companies considering going public as a credible alternative to a U.S. SPAC.

Timing is relevant. There are already over 700 SPACs currently in the market seeking to identify suitable targets at an acceptable valuation. European financial centers are behind the U.S. curve, with some participants already concerned about a SPAC bubble. Perhaps an impressive and credible sponsor team will be even more important for supporting any future SPACs in Europe.

Culture is also relevant. When considering SPACs, U.S. investors are typically less risk-averse compared to their European counterparts.

Even as London and Paris (and others such as Amsterdam and Frankfurt) seek to refine their regulatory frameworks for SPACs, given the timing and cultural factors, it is still too early to predict the ultimate size of this investor community.

The Authors:

Jeffrey M Bronheim
Partner

+44 (0) 20 8037 2320
Email Jeff

Muriel Goldberg-Darmon
Partner

+33 1 53 53 45 06
Email Muriel

Bonnie J Roe
Partner

+1 212 707 1331
Email Bonnie

Daniel H Mathias
Counsel

+44 (0) 20 8036 9402
Email Daniel

Pierre Wolman and Patrick Ferguson also contributed to this article.

About Cohen & Gresser:

Cohen & Gresser is an international law firm with offices in New York, Paris, Washington, DC, and London. We have an outstanding record of success in high-stakes and high-profile litigation, investigations, and transactional work for our clients, including major financial institutions and companies across the world. Our attorneys have superb credentials, and are committed to providing the efficiency and personal service of a boutique law firm along with the quality and attention to detail that are the hallmarks of the best firms in the world. The firm has been recognized in a wide range of publications, including *Chambers* and *The Legal 500*.

New York | Paris | Washington DC | London

www.cohengresser.com
info@cohengresser.com
+1 212 957 7600

View C&G's Profile