

## PUBLIC STATEMENT

### SPACs: prospectus disclosure and investor protection considerations

Although special purpose acquisition companies (SPACs or the issuer) are not a new phenomenon, SPAC activity in the European Union has increased significantly in the first half of 2021. While these companies may contribute to the equity financing of SMEs, it is important that SPACs also satisfy the relevant regulatory requirements. Therefore, the European Securities and Markets Authority (ESMA) is issuing this Public Statement to promote coordinated action by National Competent Authorities (NCAs) regarding the scrutiny of the disclosure included in prospectuses relating to SPACs, which are approved in accordance with Regulation (EU) 2017/1129<sup>1</sup> (Prospectus Regulation or PR).

ESMA is also issuing this statement to draw attention to the importance of the proper application of the Directive 2014/65/EU (MiFID II) product governance requirements by manufacturers and distributors of SPAC shares and warrants as a sound implementation of the existing rules and careful scrutiny of such products in firms' product approval processes is fundamental for investor protection, a key ESMA objective.

While this statement is addressed to NCAs, its content should be taken into account by issuers when drawing up prospectuses concerning SPACs and by manufacturers and distributors of SPAC shares and warrants. After the publication of this statement, ESMA and NCAs will continue to monitor SPAC activity within the Union to determine if additional initiatives are necessary to promote coordinated supervisory action aimed at preserving investor protection.

### Background

SPACs are shell companies that are admitted to trading on a trading venue with the intention to acquire a business and are often referred to as *blank check companies*. The persons responsible for setting up SPACs are the sponsors, who typically have significant expertise in one or more economic sectors and use the SPAC to acquire companies in those sectors. SPACs sell their shares, often together with warrants, to investors to finance the acquisition.

The life cycle of a SPAC is typically divided into three phases:

1. The first stage is the Initial Public Offering (IPO), whereby the shares and warrants in the SPAC are admitted to trading on a trading venue;

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<sup>1</sup> Regulation (EU) 2017/1129 of the European Parliament and of the Council of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC (OJ L 168, 30.6.2017, p. 12).

2. In the second stage, the SPAC searches for a target company to acquire; and
3. The third and final stage consists of the business combination with the target company, typically through a merger.

After the third stage, the SPAC is a *normal* listed company.

During the first stage, an approved prospectus will generally be published in relation to the admission to trading of the shares on a regulated market and/or in relation to any offering to the public of such shares. As regards the third stage (i.e. the acquisition of the target company), it is possible that no approved prospectus will be published in relation to the business combination unless required under the Prospectus Regulation. Where no approved prospectus is provided to investors at this stage, ESMA has some concerns in relation to the disclosure provided by SPACs on the business combination. Such information would typically consist of what is presented to the shareholders' meeting when it is asked to approve the business combination and may not meet the standards which would normally be expected and verified by an NCA when a new business is admitted to trading on a regulated market or where shares are offered to the public.

### **The complexity of SPAC shares and warrants**

ESMA notes that the structure of SPAC transactions is complex and there may be variations between transactions. Furthermore, differences in company law and market practices in jurisdictions mean that investors need to study the structure of SPAC transactions carefully to ensure that they understand the transaction. In that regard, ESMA places significant importance on the comprehensibility and comparability of SPAC prospectuses and therefore has decided to publish this statement to promote uniform disclosure. ESMA considers that SPAC transactions may not be appropriate investments for all investors due to their complexity because of factors such as the risks related to dilution, incentives issues for sponsors, the different way costs of underwriting fees may be borne by SPAC redeeming investors and remaining investors, as well as uncertainty as to the identification and, subsequently, the evaluation of target companies.

ESMA notes that SPAC shares and warrants are, amongst other things, subject to the MiFID II requirements on product governance. ESMA notes that, in light of the risk and complexity of SPAC shares and warrants, it expects manufacturers and distributors of SPAC shares and warrants to carefully scrutinise such products in their respective product approval process in order to assess whether retail clients<sup>2</sup> should be excluded from the positive target market or even included in the negative target market<sup>3</sup>.

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<sup>2</sup> Within the meaning of Article 4(1)(11) of MiFID II.

<sup>3</sup>Target market of the SPAC shares and warrants (the shares of the company emerging from the business combination of the SPAC with the target company might have a different and potentially wider target market).

## The disclosure requirements for prospectuses relating to SPACs

ESMA considers that some of the applicable disclosure requirements included in Commission Delegated Regulation (EU) 2019/980 (CDR 2019/980) are likely to have particular significance when determining whether a prospectus relating to SPACs includes all the necessary information to allow an investor to make an informed investment decision, as required under the Prospectus Regulation. Therefore, without prejudice to the other applicable disclosure requirements in Annexes 1 and 11 of CDR 2019/980, ESMA encourages NCAs to focus their scrutiny of SPACs prospectuses on the following disclosure requirements:

### 1. Risk factors

*The risk factors concerning both the issuer and its securities, taking into account the conflicts of interest inherent to SPAC transactions<sup>4</sup>, the governance of the SPAC, the decision-making process concerning the business combination and any possible future dilution, such as dilution arising from the payment of the sponsors' fees in shares, the exercise of warrants and/or in relation to the financing of the acquisition.<sup>5</sup>*

Due to the complexity of SPAC transactions, NCAs should ensure that issuers provide an overview of the amount of possible dilution in different scenarios by using a table or diagram.

### 2. Strategy and objectives

*A description of the issuer's business strategy and objectives, both financial and non-financial (if any). This description shall take into account the issuer's future challenges and prospects.<sup>6</sup>*

NCAs should ensure that issuers provide detailed information about the issuer's investment policy/strategy, and the criteria for the selection of the target company. Furthermore, NCAs should ensure that this investment policy/strategy is consistent with the rest of the information in the prospectus. For example, if the issuer intends to invest in a 'green' target or a tech company but is also able to select a target outside of these sectors, the name of the issuer should not imply that it will only invest in ESG or tech companies.

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<sup>4</sup> Common conflicts of interests inherent in SPAC transactions are set out below under, 'Conflicts of interest – sponsors'.

<sup>5</sup> Item 3.1 of Annex 1 and Item 2.1 of Annex 11 to CDR 2019/980.

<sup>6</sup> Item 5.4 of Annex 1 to CDR 2019/980.

### 3. Escrow accounts and the reinvestment of the proceeds

*Information on the funding structure of the issuer.<sup>7</sup>*

NCAAs should confirm that the prospectuses contain information about any escrow account or the reinvestment of the proceeds of the offering in the period before the acquisition of the target company, including any reliance on third parties and/or investment policy.

### 4. Relevant experience and principal activities of the administrative, management and supervisory bodies

*An indication of the principal activities performed by the members of the administrative, management and supervisory bodies outside of that issuer where these are significant with respect to the issuer, as well as each member's relevant management expertise and experience.<sup>8</sup>*

### 5. Conflicts of interest - sponsors

*Information on conflicts of interest.<sup>9</sup>*

In particular, NCAAs should check that the prospectus discloses any conflicts of interests arising under the following situations:

- i. in the event that the sponsors will lose their initial investment if no acquisition is completed by a specific deadline;
- ii. in relation to any agreements with the sponsors restricting their disposal of the issuer's securities;
- iii. concerning any possibility that the SPAC could invest in companies associated with the sponsors;
- iv. relating to the fact that the sponsors and their affiliates may have already invested in the same sector as the SPAC; and
- v. emerging due to the fact that the sponsors and their affiliates are not obligated to share any potential targets they identify with the SPAC and may acquire these targets themselves.

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<sup>7</sup> Item 8.3 of Annex 1 to CDR 2019/980.

<sup>8</sup> Item 12.1 of Annex 1 to CDR 2019/980.

<sup>9</sup> Item 12.2 of Annex 1 to CDR 2019/980.

## 6. Shares, warrants and shareholder rights

*Detailed information on the share and warrant structure, including information on any redemption, withdrawal rights and information about any rights that the shareholders meeting must approve concerning acquisition of the target company.<sup>10</sup>*

NCAAs should ensure that detailed information is included in prospectuses concerning the procedure for approving the business combination in the shareholders' meeting, including the required majority for its approval.

Additionally, NCAAs should ensure that prospectuses contain a detailed description of the disclosure that the issuer will provide to the shareholders' meeting about the target company and the ensuing business combination, especially if it is possible that no approved prospectus will be presented to investors concerning the business combination. Such disclosure will enable investors to assess whether they are comfortable with the level of disclosure that will be provided in relation to the business combination in the future. In that regard, NCAAs should ensure that SPACs provide investors with, in relation to the business combination, a level of disclosure similar to that included in an approved prospectus.

## 7. Major shareholders

*Information about major shareholders.<sup>11</sup>*

This information should include

- i. the name of any person other than a member of the administrative, management or supervisory bodies who, directly or indirectly, has an interest in the issuer's capital or voting rights which is notifiable under the issuer's national law, together with the amount of each such person's interest or, if there are no such persons, an appropriate statement to that effect that no such person exists; and
- ii. information as to whether major shareholders have different voting rights or an appropriate statement to the effect that no such voting rights exist.

## 8. Related party transactions

*Information about any related party transactions.<sup>12</sup>*

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<sup>10</sup> Items 19.1.4, 19.1.5, 19.1.6, Item 19.2.2 and 19.2.3 of Annex 1 and Item 4.5 of Annex 11 to CDR 2019/980

<sup>11</sup> Items 16.1 to 16.4 of Annex 1 to CDR 2019/980.

<sup>12</sup> Item 17.1 of Annex 1 to CDR 2019/980.

## 9. Material interests

*Information about any material interests in the SPAC transactions, including conflicts of interest.*<sup>13</sup>

NCAAs should ensure that issuers disclose any services provided to the issuer by parties associated with the sponsors.<sup>14</sup>

## 10. Information on the proceeds of the offer

*If the issuer is aware that the anticipated proceeds will not be sufficient to fund the entire acquisition, the issuer should include an estimation of the amount and sources of other funds needed, including further details about the proceeds since they are being used to acquire the target company.*<sup>15</sup>

NCAAs should ensure that the prospectus includes information about the financing of the acquisition of the target company in the event that the proceeds do not cover the entire acquisition price. It may be necessary to provide information on different scenarios to provide investors with sufficient information to make an informed investment decision.

Equivalent information should also be provided in relation to the shares and the warrants placed with the sponsors, since the proceeds of such placement are often used to fund the SPAC during the period before the acquisition of the target company. This information should enable investors to assess the total level of costs during the period up to and including the acquisition of the target company and whether there is any risk that the amounts intended to fund such costs are likely to be insufficient.

## 11. Information on the intention of certain persons to subscribe in the offer

*An indication of whether major shareholders or members of the issuer's management, supervisory or administrative bodies intend to subscribe in the offer, or whether any person intends to subscribe for more than five per cent of the offer*<sup>16</sup>.

## 12. Information on the offer price

*Any material disparity between the public offer price and the effective cash cost to members of the administrative, management or supervisory bodies or senior management, or affiliated persons, of securities acquired by them in transactions during the past year, or which they have the right to acquire.*<sup>17</sup>

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<sup>13</sup> Item 3.3 of Annex 11 to CDR 2019/980.

<sup>14</sup> Item 3.4 of Annex 11 to CDR 2019/980.

<sup>15</sup> Item 3.4 of Annex 11 to CDR 2019/980.

<sup>16</sup> Item 5.2.2 of Annex 11 to CDR 2019/980.

<sup>17</sup> Item 5.2.3 of Annex 11 to CDR 2019/980.

### **Additional disclosure likely to be required to satisfy the PR**

Furthermore, in order to foster convergence among NCAs regarding the scrutiny of SPAC prospectuses, ESMA considers it appropriate that NCAs ensure that additional elements are included. This should help to make certain that SPAC prospectuses contain the necessary information to allow an investor to make an informed assessment of the issuer and the securities to ensure compliance with the PR. In this respect, ESMA notes that NCAs may require the inclusion in the prospectus of supplementary information, where necessary for investor protection.

For example, ESMA is of the opinion that NCAs should generally expect the following disclosure to be included in SPAC prospectuses:

- i. the future remuneration of the sponsors and their possible role after the acquisition of the target company;
- ii. information about the future shareholdings of the sponsors and other related parties;
- iii. information about possible changes to the governance after the acquisition of the target company; and
- iv. detailed information about the possible scenarios that may arise if the sponsors fail to find a suitable target to acquire, including possible scenarios such as the winding up of the issuer and de-listing of the shares.

ESMA recognises that the disclosure in the IPO prospectus may differ depending on the applicable company law and market practices. As such, this list is not meant to be exhaustive and NCAs may require additional disclosure for the purposes of investor protection.