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Strong demand for Special Purpose Acquisition Companies continues

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The following interview with BVI partner Michael Killourhy was first published by Hedge Week on 26 November 2019.

With record setting years in 2017 and 2018 for Special Purpose Acquisition Company (SPAC) offerings in the United States, strong demand continued into 2019. SPAC IPOs crossed the 100 mark by end Q2 2019. SPACs are publicly-traded investment vehicles that raise funds via an IPO to complete a targeted acquisition (a "business combination") within a limited time frame (18-24 months).

The funds raised are placed in an interest bearing trust account and may only be used to fund a business combination. If the company fails to complete a business combination, the funds are returned to investors with interest (by the redemption of their shares). Investors also have the option to redeem their shares on the same terms immediately before a business combination.

SPAC offerings are structured as sales of "units" comprising common equity and derivative securities (usually warrants exercisable following a business combination and/or "rights" that convert into shares on a business combination). The units will initially trade as a single security, but later their components will trade separately.

SPAC units can offer unique investment opportunities. For hedging or yield-focused strategies, the assured redemption return of SPAC shares, backed by the trust account, offers a relatively attractive yield (SPAC shares typically trade at a discount to their fixed redemption price) with very low risk. Unlike comparable hedges such as US Treasuries, SPAC units also include, through their component warrants or rights, a free option to participate in the post business combination undertaking – which can survive even if the investor elects to redeem its shares before close. SPAC warrants also offer opportunities for more aggressive strategies. The warrants will expire worthless if the SPAC fails and are priced accordingly by the market, while most institutional investors eschew the risk, its pricing can still be compelling to others.

For targets, SPACs offer an alternative means of accessing growth capital. The prestige of listed status is also important– as it was for China Direct Lending when acquired by the SPAC DT Asia Investments in 2016 to become the first Nasdaq listed Chinese finance business.

SPACs remain popular with Chinese sponsors for linking domestic businesses into US listings, notwithstanding trade tensions and recent SEC rule changes. Continued Chinese interest in SPACs is also welcome for British Virgin Islands entities. While most US listed SPACs are Delaware corporations, for non-US sponsors seeking targets outside the US, a vehicle incorporated outside the US might offer more efficient post acquisition structure. The SEC also allows rules concessions for non-US issuers which qualify as “Foreign Private Issuers”. For non-US sponsors, particularly Chinese sponsors, the BVI has become a preferred jurisdiction.

The BVI’s appeal has several factors, including the SPAC suitability of BVI company law, tax neutrality and the similarities between aspects of the BVI and Delaware company statutes. BVI SPACs are also pioneers, features such as “rights”, “fractional warrants” and the ability to extend SPAC life spans were used in BVI SPACs several years ago. The first India focused SPAC in recent years was a BVI company, as was the SPAC that facilitated the first ever Nasdaq listed Chinese finance business, and in 2018 a BVI SPAC, National Energy Services Reunited Corp, completed a unique simultaneous double business combination when it acquired two Middle Eastern oil businesses with a combined value over USD1.1 billion.

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