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SPAC LISTING REGIME CONSULTATION

Special purpose acquisition company (the "**SPAC**") offerings have recently risen in popularity in global public offering (the "**IPO**") markets. In September 2021, The Stock Exchange of Hong Kong Limited (the "**Stock Exchange**") issued a consultation paper to solicit market feedback on proposals to amend the Rules Governing the Listing of Securities on the Stock Exchange (the "**Listing Rules**") to create a listing regime for SPACs in Hong Kong. In this issue, we will go through the key proposals of the consultation.

Background

A SPAC is a special purpose shell company that raises funds through an IPO for the purpose of later merging with a private operating company (the "**SPAC Target**"). As SPACs have to complete its acquisition of a business ("**De-SPAC Transaction**") within a pre-defined time period after its listing (usually within two years), SPACs will have to actively search for private companies that they wish to acquire.

SPACs do not have any business operations and do not have assets other than the proceeds from IPO. The funds raised will be used as consideration when acquiring a SPAC target company. SPACs will be managed by qualified professionals who have private equity, corporate finance and/or relevant industry experience ("**SPAC Promoters**"). The shareholders in a SPAC are investing based on the trust in the SPAC Promoters to find a suitable SPAC Target, which would benefit from the SPAC Promoters' expertise and drive returns to shareholders.

Listing via a SPAC is often perceived to be an attractive alternative to a traditional IPO due to the shorter timeframe for listing along with a higher degree of price certainty and flexibility in structuring a De-SPAC Transaction.

The introduction of a SPAC listing regime in Hong Kong could potentially attract companies within Asia to list in Hong Kong through a SPAC structure. In order to ensure the quality of the SPAC Targets, it is crucial to have necessary safeguards in place. The Stock Exchange has therefore issued a consultation paper with a view to create a listing regime for SPACs in Hong Kong.

SPAC Listing Regime proposed by the Stock Exchange

To avoid an over-supply of SPACs seeking acquisition targets, the Stock Exchange has proposed a rather stringent approach to SPAC listings. Set out below are the key proposals of the Stock Exchange for the SPAC listing regime:-

(i) Investor suitability

The subscription and trading of a SPAC's securities will be restricted to Professional Investors (as defined in the Securities and Futures (Professional Investor) Rules) only. A SPAC must issue and allot both the SPAC shares and SPAC warrants to a minimum of 75 professional investors, of which 30 must be institutional professional investors.

(ii) Trading arrangement

Separate trading of SPAC shares and SPAC warrants must be in place from initial offering date, with additional measures to mitigate the risk of volatility associated with the trading of SPAC warrants.

(iii) SPAC Promoters and dilution cap

SPAC Promoters must meet suitability and eligibility requirements, including the requirement for each SPAC to have at least one SPAC Promoter to be a firm that holds (a) a Type 6 (advising on corporate finance) and/or a Type 9 (asset management) license issued by the Securities and Futures Commission (the "**SFC**"); and (b) at least 10% of the promoter shares. Promoter shares must not exceed 30% of the shares the SPAC has in issue as at the initial offering date.

(iv) Fund raising size

Total funds raised by a SPAC from its initial offering must exceed HK$1 billion.

(v) New listing application and forward-looking information

The successor company upon the completion of a De-SPAC Transaction (the "**Successor Company**"), will need to meet all new listing requirements (including the engagement of sponsor, due diligence requirements, minimum market capitalisation requirements and financial eligibility tests). Application of existing requirements on forward-looking statements in the listing document for a De-SPAC Transaction shall be of the same as that required for an IPO (including the requirement for reports from the reporting accountant and IPO sponsor on such statements).

(vi) Independent third-party investment

Independent third party investments must (a) constitute at least

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25% of the expected market capitalisation of the Successor Company (or at least 15%, if the Successor Company's expected market capitalisation at listing is over HK$1.5 billion); and (b) result in at least one asset management firm or fund (with assets under management/fund size of at least HK$1 billion) beneficially owning at least 5% of the issued shares of the Successor Company as at the date of the Successor Company's listing.

(vii) Shareholder vote

A De-SPAC Transaction must be made conditional on the SPAC shareholders' approval at a general meeting. A shareholder with a material interest in the transaction will have to abstain from voting, and if the De-SPAC Transaction results in a change of control, any outgoing controlling shareholders of the SPAC and their close associates must not vote in favour of the De-SPAC Transaction. SPAC shareholders must be given the option to redeem their shares prior to any of the following: (i) a De-SPAC Transaction; (ii) a change in SPAC Promoter; and (iii) any extension to the deadline for finding a suitable De-SPAC Target.

(viii) Open market in Successor Company's shares

A Successor Company must ensure an adequate spread of holders of its shares of at least 100 shareholders.

Potential benefits of a SPAC listing regime in Hong Kong

Under the proposed SPAC regime, investors may choose to either redeem their investment prior to the De-SPAC Transaction or continue with the investment after assessing the potential return of the SPAC Target. Funds raised by a SPAC in its IPO will be held in a third-party trust account until a De-SPAC Transaction occurs or until the SPAC is liquidated for not having completed such a transaction within a set period of time. SPAC shareholders will be given the opportunity to consider the terms of a De-SPAC Transaction proposed by the SPAC Promoter and vote on the relevant resolutions at a general meeting.

One of the potential benefits of listing via a SPAC may be the time and cost efficiency due to the streamlined SPAC listing process. The process for a De-SPAC Transaction listing could be as short as three months, substantially shorter than the twelve months generally required for a traditional IPO. In addition, SPAC Targets are able to compromise on a suitable valuation with the SPAC Promoter which means that there is a greater control over the pricing/valuation process and additional certainty. The terms of the De-SPAC Transaction, including but not limited to, the funds raised, compensation for dilution and management incentives can also be adjusted to tailor to the requirements of the SPAC Target to a level of flexibility which would not be possible for a typical IPO.

Conclusion

SPAC has attracted much more attention globally in the 2020 US SPAC frenzy. SPAC activity has spiked as investors seek the next high growth opportunity. However, the US SPAC frenzy has cooled significantly since the second quarter of 2021 as the Securities and Exchange Commission issued multiple alerts, statements and guidance notes. The proposed SPAC listing regime could potentially bring about a new wave of new listings to the Hong Kong markets, as having been demonstrated through the implementation of the 2018 listing reforms that enabled the listings of biotech companies, issuers with weighted voting right structures and secondary "homecomings". As the Hong Kong financial market is already considered to be a compliance minefield by many, companies wishing to go public in Hong Kong via a SPAC should consider seeking financial advice from experienced professionals at an earlier stage to avoid regulatory issues.

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