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Discours de Benoît de Juvigny, Secrétaire général de l'AMF - IOSCO SPAC Network Stakeholder Meeting - 16 décembre 2021 (en anglais uniquement)

Seul le prononcé fait foi

Introduction

Delighted to participate in this IOSCO outreach event dedicated to the topic of SPACs. Acknowledgements to the Chair, Jean-Pierre Servais, for the invitation. Thanking IOSCO and all members and affiliates connected around the world, good to see – though virtually – so many people involved in the topic of SPACs. SPACs are a topic that is of particular interest to me, firstly as Secrétaire général of the AMF and secondly as chair of ESMA CFSC. We have devoted significant efforts and time in France and at ESMA on this topic, to monitor and support these transactions, while ensuring appropriate investor protection. I have been tasked by Jean-Paul to introduce this afternoon's discussion, so I will try to briefly set the scene and give an overview of some of the questions raised related to SPACs.

Context: Market Trends

As everyone knows, the hallmark of the financial markets in 2020 and 2021 has undoubtably been the spectacular rise in the number of SPAC transactions and amounts raised. Although a slowdown has been observed since the beginning of the second semester of 2021, the development of SPACs will certainly continue in 2022 and onwards. On this point, it should be noted that SPACs are not entirely new, having existed for 30 years in the

US. Nonetheless, it is only in recent years that there has been a significant rise of such transactions. In my view this trend should not be viewed as transitory, but as a long-term phenomenon, showing that market players are continually looking to optimise the IPO process as the latter has become more complex over the years, in order to achieve a faster and a less risk prone listing process for companies.

The trend is most evident in the US of course as the leading global market of SPACs, where there have been twice as many operations compared with the whole of the previous year, which already saw an increase from circa 60 to 250 SPACs compared to 2010. As reported by Garry Gensler recently, "the number of SPAC blank-check IPOs has ballooned in the US by nearly 10 times between 2019 and 2021. Further, those SPAC blank-check IPOs now account for more than [60%] of all U.S. IPOs"(1). This shows that SPACs are clearly an important alternative for the listing of corporations in addition to traditional IPOs.

The trend has also been true, but to a lesser extent, in Europe where we have seen 26 SPACs raising a total of close to 6 billion Euros up to September this year, with transactions being made in multiple Member States, including Netherlands, France, Germany, Italy, Luxembourg and Sweden. This is in comparison to circa 500 million euros raised last year.

In France, the AMF approved five SPACs in the last 12 months, marking a clear increase in activity.

From a macroeconomic perspective, it has been argued that the abundant liquidity and diminishing returns on traditional instruments have pushed investors towards more diversification, seeking access to companies with high growth potential, which are not always public.

It is interesting to note that we have also seen, in the aftermath of Brexit, a touch of regulatory competition among jurisdictions looking to stimulate their local financial markets and attract new market players and transactions. With this soft competition happening in the background, market players tend to compare the different applicable regimes for listing and incorporating SPACs in specific jurisdictions in order to optimise for the transaction's considerations, which can vary on a case by case basis. This justifies the increased level of cooperation that we have seen among authorities in different jurisdictions, with a general goal to limit any regulatory arbitrage that could facilitate excesses.

Experience and Risks Relating to SPACs

SPACs are generally compared to traditional IPOs and are praised as an alternative for non-listed companies to enter the public markets. They are a way to bring the worlds of private

equity and the public markets together, allowing the listing of companies that might otherwise remain private, opening the opportunity to buy shares and participate in their returns to a much wider investor audience.

From the point of view of the target company, the process has a number of virtues. It is considered as safer, cheaper and more efficient than a traditional IPO. In particular, it is seen as safer because the valuation of the target company does not depend on volatile and rapidly evolving market conditions which can jeopardise an IPO: the equivalent risk of a SPAC acquisition not going through because of lack of SPAC investor support is generally considered lower than the volatility risk in traditional IPOs. It is also considered a cheaper alternative to the traditional IPO because the target does not itself directly bear the costs of the SPAC's listing, those costs being absorbed for the most part by investors and existing shareholders via the dilutive effects embedded in SPACs. It is also seen as more efficient because the IPO process can take longer than a SPAC M&A, and the management of the target company might be less disrupted in the case of a SPAC acquisition than a market acquisition.

However, from the investor perspective, including existing shareholders of the target company, that remain, it has been shown that such transactions are not always profitable, as those investors will need to in fine absorb the significant dilutive effects of the SPAC (2), which typically cover costs related to sponsors' remuneration, therefore creating an uneven distribution of returns between stakeholders, and potentially other costs related to the SPAC structure and listing. Investors might also suffer from an under-performance of the combined company after the acquisition, as observed in some recent transactions.

Often times the SPAC needs additional funding at the time of de-SPACing in order to acquire the desired target, typically recurring to "private investment in public equity" (PIPE) mechanisms whereby additional investors are called upon to provide additional funding and replace redeeming initial investors. These investors are typically invited to join at a time when the target is known. They thus have the advantage of deciding to invest based on a significantly more complete information picture than the initial SPAC investors, although it is worth noting that initial investors have the possibility to jump out via their redemption right if they don't agree with the target choice.

Behind the mentioned perceived advantages, the exponential surge of SPACs has not been without consequences on the proper functioning of the markets, namely in the US. For example, the incentives of sponsors embedded in the structure of these vehicles and the pressure to find targets within the defined timeframe in a context of fierce competition between SPACs generated excesses and concern.

Misalignment of interests between sponsors and other investors have been notably observed at the time of de-SPACing, the sponsors sometimes seeking to strike a deal at any cost, potentially irrespective of the deal quality and without appropriate due diligence. Litigations or investigations have ensued in the US, revealing fraud or false information provided to the market on the robustness of the target companies' business or performance. In a number of instances, SPAC valuations dropped significantly post de-SPACing, pointing to the mentioned excesses.

It is thus important to properly manage potential conflicts of interest in order to avoid a crystallisation of interest misalignment between sponsors and other investors in the SPAC. One form of such conflict of interest is when a sponsor has pre-existing ties and business interests in the sector of activity targeted by the SPAC. It is easy to see how such sponsors may be incentivised to choose targets and make deals favouring own interests, potentially to the detriment of those of other investors.

In addition, and in contrast to traditional IPOs, SPACs have an important marketing aspect attached to them that can easily lead to undesirable outcomes, with loose statements and overly optimistic financial projections that were observed in some cases. We have also seen certain sponsors leveraging their notoriety, not always business-related, in order to ensure a following among investors, sometimes retail investors.

This is why authorities and other stakeholders must pay close attention to specific disclosure issues, for example on forward looking statements and on the dilutive effects of these transactions, with a focus on investor protection.

Regulatory Initiatives

On the regulatory side, globally, the mobilisation and cooperation among market authorities, exchanges and sometimes legislators was almost unprecedented in 2021. In the US, communications and actions undertaken by the SEC, but not only, clarified, improved or reinforced the existing regime, and continues to do so, with the aim to regulate the development of SPACs, to provide improved safeguards and to balance the level playing field compared to traditional IPOs.

In other jurisdictions, initiatives generally intended to support or permit the use of SPACs locally, and ensure that, despite their complexity and risks, SPACs could develop and thrive in a healthy manner within their domestic markets, recognizing that these transactions are a clear alternative to more traditional methods of raising capital.

As mentioned, market authorities as well as market participants strived to mitigate related concerns. They did so in different but often similar manners.

They can seek to improve disclosure and transparency requirements (3) in order to ensure adequate investor information, both at the time of the SPAC's listing and upon de-SPACing.

Before approving a transaction, they can require issuers to address the identified conflicts of interest. Mitigations can include the introduction of a redemption right for investors that disagree with the choice of the target (allowing them to cancel their initial investment), although there can be variations on how redemption rights work in practice. Additional limits regarding the decision to approve the target can also be required, such as excluding sponsors from the voting process once a target is found.

It is often required, at least as a market practice, that funds raised by a SPAC be deposited in an escrow account until the target acquisition. Measures can be taken to limit retail access to SPAC offerings. There can also be a requirement for a minimum amount that needs to be raised by the SPAC, which can prevent small transactions of this type from proliferating, as they are often times correlate with less scrupulous practices.

Other specific issues that are still debated include considerations with respect to the appropriate accounting treatment of the financial instruments issues by these vehicles. In April 2021 the SEC published a statement (4) concluding that warrants issued by SPACs should be classified under US GAAP as debt, measured at fair value, instead of equity. Some have argued that this statement has contributed to damping the market of SPAC in Q2 2021. In Europe, ESMA raised an issue (5) to the IFRS IC in order to require clarifications from the standard setter interpretation committee on the application of the existing requirements under IFRS (IAS 32) in relation to the classification of shares issued by SPAC on balance sheet. In particular the question raised is whether and under what circumstances shares issued by the SPAC should be classified as liabilities or as equity instruments given the right of redemption of shareholders both in the event of an acquisition, depending on how the acquisition decision is made, and in the event of liquidation.

At the same time we are seeing market practices evolving in order to accommodate on the one hand regulators' concerns and on the other investors' expectations. Examples include the increase of lock-up periods of founders' promote, the decrease of the promote's size as well as the tethering of sponsors' remuneration to the target's performance.

European Regulatory Perspective

From a European perspective and taking my role as chair of the CFSC at ESMA, a few words on ESMA's efforts to contribute to maintaining a high level of investor protection and promote a common consistent supervisory convergence across the EU.

ESMA released in July of this year, under the auspices of CFSC, a statement (6) aimed firstly at drawing attention on the fact that SPAC transactions may not be an appropriate investment for all investors due to their complexity and the risks attached. The statement sets out recommendations both (i) with respect to the proper application of product governance and distribution of shares and warrants under the MIFID II, and (ii) with respect to specific disclosures that are expected under the Prospectus Regulation, to improve the comprehensibility and comparability of SPAC prospectuses. The statement aims also to coordinate and promote a convergent approach by NCAs on the scrutiny of SPAC prospectuses. ESMA will of course continue to monitor the SPAC activity.

What's next at European level? As you all know, the European Commission has launched a public consultation on "making public capital markets more attractive for EU companies and facilitating access to capital for SMEs" (7). This consultation includes questions on the appropriateness of the current listing regime as regards IPOs via SPACs. It asks for example if there is a need to reinforce safeguards or better harmonise disclosure regimes in the EU.

Approach with respect to SPACs and Lessons Learned in France

With a high-quality structure that allows for alignment of interests, SPACs can be a proper way of introducing companies of a certain size on the stock exchange, complementing the traditional IPO process and establishing a potentially fruitful link with private equity.

As expressed in its press release in April of this year (8), the AMF was rejoiced to welcome new SPACs on the regulated market in the context of existing European legislation that allows for such transactions without the need for a dedicated framework.

We were also rejoiced to see that the market infrastructure in Europe was particularly well equipped and proved to be sufficiently robust to handle the listing of units on the regulated market, composed of shares and warrants.

We are convinced at the AMF that having a sufficiently flexible but robust regulatory framework allows market practice to pursue its evolution and adjustment, in particular as investors start gaining more leverage in negotiations, as we have seen after the initial period of euphoria early this year.

For example, in more recent transactions the previously generous remuneration package that was granted to sponsors is now becoming more constrained and is more carefully negotiated, with for example progressive remuneration of sponsors subject to, in part, financial targets for the combined company.

On the disclosure side, the Prospectus Regulation can be seen as fit for purpose as it currently stands. Upon instruction of new SPACs, the AMF has generally ensured that specific disclosure aspects were properly addressed within the Prospectus Regulation framework. The AMF was particularly attentive to disclosures related to sponsors' conflicts of interest and their mitigation, the targets' sector of activity, investors' rights and the approval process of the target company. Adequate disclosures on the target company upon de-SPACing are also expected.

From the point of view of investor protection, in practice, retail participation has not been an issue for SPACs listed in France. On the primary market, retail investors are de facto excluded from SPACs' IPOs because, in practice, SPACs have been listed via private placements reserved to qualified investors and with increased minimum subscription amounts. It is worth noting that having fewer small investors also facilitates the de-SPACing process especially when shareholders are granted a voting right with respect to the target, easing the handling of confidentiality and market abuse considerations from a practical standpoint, as well as potentially diminishing the risk of high redemption rates, effectively facilitating the unfolding of these transactions. On the secondary market, French SPACs have been listed on Euronext's Professional Segment, where retail access is restricted (but not impossible) and for which specific MIFID distribution and product governance rules apply.

From our experience, there is a general agreement on the fact that SPACs, due to their complexity and inherent uncertainties, should not target retail investors, and that only professional investors should have access to SPAC offerings. Having a Professional Segment with barriers to the entry for retail investors and specific MIFID product governance rules strikes a good balance between investor protection and the promotion of public markets as a financing channel.

It was also our experience that the facilitating of the dialogue between the sponsors and professional investors ahead of a SPAC IPO is key to promote a balanced agreement between sponsors' rights (ie. the size of the promote) and investor protection (ie. deadline for the acquisition to be completed, expected content of the information to be release ahead of the redeem decision). The non-written agreement between the sponsors and professional investors is then transposed in a prospectus that needs to be approved by the AMF before being publicly released.

Closing Remarks

As we have seen, there are different realities on the SPAC markets around the world. Some jurisdictions have dealt with SPACs for decades, benefiting from developed market practices, while other countries have only recently seen a development locally. These different levels of maturity come with other disparities, for example, regarding the size and the structure of the operations, the practices around listing, the issues encountered, as well as more broadly the regulatory environment. A “one size fits all” approach might therefore be very difficult to define and implement.

We have however also seen that there are many commonalities, namely in terms of key concerns, investor protection goals and safeguards. This is an opportunity to collectively pursue the monitoring of SPAC activity globally.

Particularly, we will need to continue monitoring the outcome of the numerous SPACs that are now on the market and that are looking for targets globally, as this could potentially cause excessive valuations in some scenarios.

Importantly, we must also assess the proper equilibrium that we want to target between traditional IPOs and SPACs, and consider whether the tendency should be to revise IPO requirements or to reinforce SPAC safeguards, and ensure an increased level playing field between the two.

Mots clés

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