CONYERS | British Virgin Islands

BVI SPACS

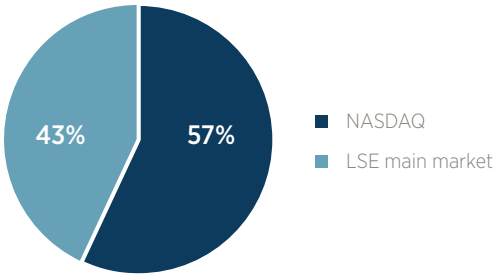
The Rise of BVI Special Purpose Acquisition Companies

There has recently been a resurgence of interest in special purpose acquisition companies (SPACs), which are also known as 'blank check' or 'cash shell' companies. Over the past 7 years SPACs incorporated in the British Virgin Islands (BVI) have raised aggregate capital of over US$5 billion and, in 2017 alone, new BVI SPACs raised gross proceeds of approximately US$2.5 billion[1]. This article outlines the key features of a SPAC, explores recent market trends and explains why the BVI is a popular domicile for these vehicles.

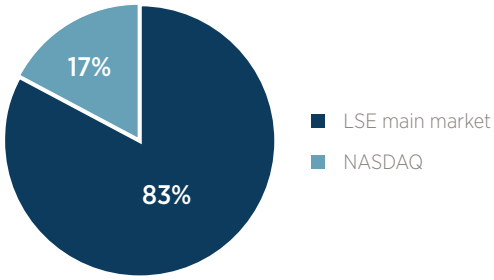
	Notable BVI SPACs	Year of listing	Amount Raised
NASDAQ	BGS Acquisition Corp	2012	$40,000,000
	DT Asia Investments Limited	2014	$60,000,000
	Atlantic Alliance Partnership Corp	2015	$86,250,000
	Electrum Special Acquisition Corporation	2015	$172,500,000
	Pacific Special Acquisition Corp	2015	$57,500,000
	Bison Capital Acquisition Corp	2017	$60,375,000
	National Energy Services Reunited Corp	2017	$229,170,000
	Constellation Alpha Capital Corp	2017	$143,750,000
LSE	Justice Holdings Limited	2011	£900,000,000
	Atlas Mara Co-Nvest Limited	2013	$325,000,000
	Nomad Holdings Limited	2014	$485,000,000
	Ocelot Partners Limited	2017	$418,000,000
	Landscape Acquisition Holdings Limited	2017	$484,250,000
	J2 Acquisition Limited	2017	$1,250,000,000

[1] All data herein is based on BVI SPACs listed on NASDAQ and London Stock Exchange (LSE) main market during the period 1 January 2011 to 31 December 2017, and stated averages are by incidence of listings (not weighted averages).

Listing Markets by Number



Listing Markets by Capital Raised



Characteristics of a SPAC

A SPAC is a newly-formed company which raises capital by way of an initial public offering (IPO) for the purpose of using the proceeds to acquire or merge with one or more existing operating businesses. The unique and defining feature of a SPAC is its model of 'raising equity capital upfront by way of IPO to buy operating businesses later'. At the time of its IPO, the listing vehicle has no portfolio investments or substantive operations (or even any earmarked for acquisition[2]). Upon listing, all or most[3] of the net capital proceeds are placed into a third party escrow/trust account[4] and the SPAC then has a mere 12-36 months[5] in which to source and consummate a transaction (failing which the venture must be wound-up and funds must be returned to investors[6]).

For investors who buy shares in the IPO, an investment in a SPAC constitutes a bet on the ability of the SPAC's experienced (and often high-profile) management team to quickly identify and consummate attractive investment opportunities – referred to as 'business combinations' - following its listing. A SPAC provides investors with access to the type of 'buy-out' investment strategy typically restricted to private equity funds, while at the same time providing a degree of liquidity in that the shares of the SPAC are publicly traded. Further, the matching warrants issued in a typical SPAC structure provide potential equity upside for investors. If no business combination is consummated within the prescribed time period, capital is returned to the investors.

For the founders, a SPAC is attractive as it enables them to raise funds for a general acquisition strategy while typically providing greater flexibility and potentially superior economics than pursuing the same strategy through a private equity fund.

Once the SPAC has raised funds through its IPO and an appropriate target business has been identified, a business combination is effected that normally results in the target business being acquired by or merged into the SPAC (and therefore becoming a listed business). In recent years SPACs have been involved in transactions to acquire a number of household names, including Burger King, Iglo Foods, Jamba Juice and American Apparel.

[2] Applicable onshore securities laws and listing requirements effectively prohibit any substantive discussions with potential targets prior to the IPO

[3] At least 90% for NASDAQ listings

[4] An escrow/trust account is not required (and therefore uncommon) for LSE main market listings.

[5] A maximum of 36 months for NASDAQ listings. The primary period may be extendable with investor consent or if a binding letter of intent to consummate a business combination has been signed prior to expiry of the primary period.

[6] For NASDAQ listings, the SPAC must then return the balance of the escrow account to its public investors (i.e. to investors other than the founders such that the founders' equity in the SPAC will become worthless if a business combination is not consummated).

Comparison of SPACs and Private Equity

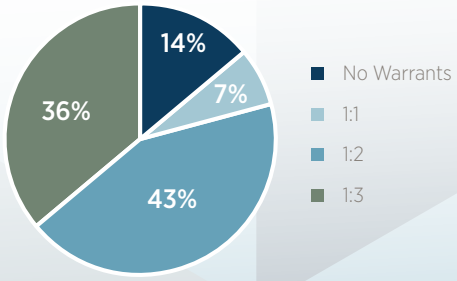
While most founders will typically have a clear idea of whether it is appropriate to establish a SPAC or private equity fund to pursue their investment strategy – not least because a SPAC is typically set-up to make concentrated acquisitions of one or a small number of businesses whereas a private equity fund will normally have a more diversified portfolio - it is instructive to compare the terms of a typical SPAC and private equity fund. The comparison is particularly interesting given that a number of private equity sponsors are now using SPACs as an alternative way of raising and deploying capital. For example, in 2017 TPG Pace Energy Holdings Corp., a SPAC formed by TPG and led by energy veteran Stephen Chazen, raised US$650 million on the New York Stock Exchange. Other prominent PE sponsors active in this space include WL Ross, Centerview Capital, Riverstone, Avenue Capital, and Avista Capital.

The following table compares the terms of a typical SPAC and private equity fund.

Choice of vehicle	
Typical SPAC	**Typical Private Equity Fund**
Company limited by shares.	Limited partnership.

Interests acquired by investors	
Typical SPAC	**Typical Private Equity Fund**
Ordinary shares (common stock) + separately tradeable equiwty warrants (one warrant per share, issued for a combined price of US$10.00)[7] Warrants are often issued on a 1:1 (full warrant), 1:2 (1/2 warrant) or 1:3 (1/3 warrant) conversion basis. The warrants are typically issued out of the money. The average warrant strike price for BVI SPAC listings has been 115% of the unit issue price (with a range of 100% - 120%). On some recent NASDAQ listings, investors have also been granted 'rights' (one right per ordinary share) to receive for nil consideration a fraction of an ordinary share (often on a 10 rights-for-1 ordinary share conversion basis) upon consummation of the initial business combination. The warrants and rights provide potential equity upside for investors and compensation in consideration for the investors' capital not being put to work pending a business combination by the SPAC.	Limited partnership interests. May or may not be unitized. No warrants or similar.

Warrant Conversion Ratio



[7] Although some SPACs have chosen not to offer any warrants at all (i.e. common stock only).

Capital raising

Typical SPAC	Typical Private Equity Fund
Capital raised upfront on public markets (and not put to work pending investment by the SPAC).	Capital commitments obtained on private markets and capital drawn down as and when required by the fund to make investments and pay expenses.

Initial use of net proceeds

Typical SPAC	Typical Private Equity Fund
For NASDAQ listings: Initially, public investors' funds are placed into a U.S.-based third party escrow/trust account pending investment or return to the public investors. The average % of investors' funds placed into escrow for BVI SPAC listings on NASDAQ has been 102% (with a range of 100% - 105%)[8]. A third party escrow/trust account is not required (and therefore uncommon) for LSE main market listings. Secondary raisings are permitted. Not possible to 'warehouse' or pre-select any investments prior to the IPO due to applicable onshore securities laws and listing requirements.	No third party escrow/trust arrangements (although limitations and restrictions ordinarily apply to any holdings of short-term investments and cash). Secondary raisings (subsequent closings) permitted during a limited period (often 12 – 18 months) post initial close. Possible in theory to 'warehouse' or pre-select a pipeline of investments prior to launch of the fund.

Mind and management

Typical SPAC	Typical Private Equity Fund
The SPACs board of directors manages the vehicle and its investment activities. The board of directors typically includes a prominent management team with extensive experience in the relevant target investment markets. No separate investment manager, general partner or similar, which keeps costs and expenses down.	The fund's general partner and investment manager manage the fund and its investment activities. The investment manager typically includes a prominent management team with extensive experience in the relevant target investment markets and/or with other financial and/or operational matters. The investment manager is almost invariably licensed to provide investment management and advisory services and therefore is subject to attendant regulatory oversight and requirements, which may add to costs and expenses.

[8] Typically any excess over 100% is funded from the sponsors' concurrent private placement.

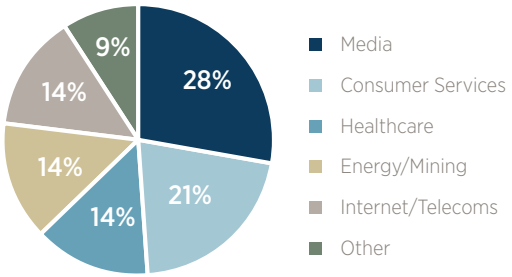
Investment mandate - asset classes

Typical SPAC	Typical Private Equity Fund
Illiquid investments, often in privately-held operating companies (or interests therein).	Illiquid investments, across a very broad spectrum of potential securities and asset classes.

Investment mandate - industries / sectors

Typical SPAC	Typical Private Equity Fund
'Target markets' may be limited to one or more specified industries/ sectors in which the management team has extensive experience. However, most SPACs have very broad discretion to invest in industries/ sectors outside of the primary 'target markets' – all BVI SPAC listings have included such additional flexibility.	Mandate may or may not be limited to one or more specified industries/sectors (although limitations and restrictions almost invariably apply).

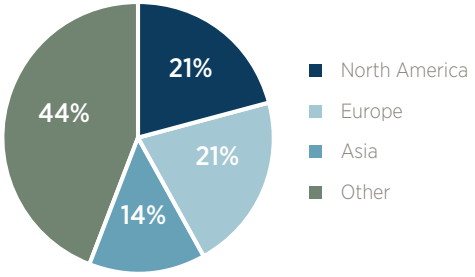
Recent BVI SPACs
Target Investment Industries



Investment mandate - geographies

Typical SPAC	Typical Private Equity Fund
'Target geographic markets' may be limited to one or more specified geographic regions in which the management team has extensive experience. However, most SPACs have very broad discretion to invest in geographies outside of the primary 'target geographic markets' – all BVI SPAC listings have included such additional flexibility.	Mandate may or may not be limited to one or more specified geographic regions (although limitations and restrictions almost invariably apply).

Recent BVI SPACs
Target Investment Geographies



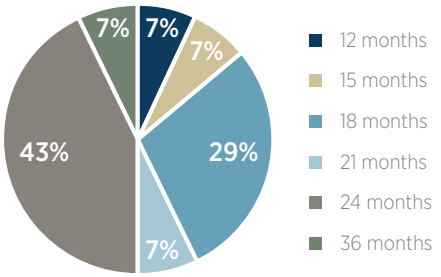
Diversification / minimum investment size

Typical SPAC	Typical Private Equity Fund
No diversification objective. SPACs often engage in only one single business combination. For NASDAQ listings: At least 80% of the escrow balance must be invested pursuant to one or more initial business combinations. No such requirement applies to LSE main market listings.	Diversified portfolio permitted (and often required, with many PE funds prohibited from making concentrated or similar investments which together constitute more than a specified % of net assets).

Investment deadline / period

Typical SPAC	Typical Private Equity Fund
SPAC must consummate one or more business combination transactions within a prescribed timeframe (often 12-36 months[9]). The average for BVI SPAC listings has been 19 months for NASDAQ and 24 months for LSE main market.	Often approximately 3-5 years, subject to potential extension in certain prescribed circumstances and exceptions for follow-on and pending investments.

Recent BVI SPACs
Investment Period



[9] A maximum of 36 months for NASDAQ listings. The primary period may be extendable with investor consent or if a binding letter of intent to consummate a business combination has been signed prior to expiry of the primary period.

Investor veto rights regarding proposed investments	
Typical SPAC	**Typical Private Equity Fund**
Earlier iterations of SPAC structures required investor approval for proposed business combinations, which created significant deal risk and made such SPACs vulnerable to activist/opportunistic investors. Now the more common construct for NASDAQ listings is either: • investor simple-majority voting approval required for a proposed business combination, with an attendant right for those investors who vote 'nay'[10] to elect to redeem out (for pro rata distributions from the balance of the escrow account) at the time of the business combination, even if the majority has approved the business combination transaction, subject to any applicable limits on conversion[11]; or • no investor vote or other approval required but with an attendant right for all investors to elect to redeem out (for pro rata distributions from the balance of the escrow account) at the time of the business combination, pursuant to a tender offer.[12] For LSE main market listings: No investor approval required in respect of proposed investments (unless otherwise required by applicable law), and no investor redemption/tender offer mechanism.	No such investor veto rights (subject to the terms of an investor's side letter regarding any 'excused' / permitted opt-out investments and certain other exceptions to mitigate tax/regulatory risks).

Investment holding period	
Typical SPAC	**Typical Private Equity Fund**
Unlimited.	Often approximately 5 – 7 years post expiry of the investment period, subject to potential extension in certain prescribed circumstances.

[10] For some SPACs, the redemption right applies even to those investors who voted 'yay', so as to reduce the risk of 'nay' votes which may otherwise block the deal.

[11] A SPAC may limit such redemption rights in respect of a given group of affiliated/related investors (to not less than 10% of the total number of shares issued in the IPO for NASDAQ listings, but often the cap is set higher) so as to prevent or limit activist/opportunistic investors from using the voting mechanism as negotiation leverage against the SPAC. The average conversion threshold for BVI SPAC listings on NASDAQ has been 19% (with a range of 15% - 20%).

[12] U.S. Foreign Private Issuers must in any event do a tender offer for any proposed business combination.

Founders' 'at risk equity'

Typical SPAC	Typical Private Equity Fund
Typically 3% - 6% of the post-IPO equity. The average for BVI SPAC listings has been 5.5% for NASDAQ and 7% for LSE main market. Founders may also advance shareholder loans for working capital purposes. Typically, for NASDAQ listings, the founders' equity is subordinated or otherwise structured such that it will be worthless if a business combination transaction is not consummated	Varies widely but often 1% - 5%.

Founders' management fees

Typical SPAC	Typical Private Equity Fund
Typically no management fees or other material compensation pending investment.	Often approximately 1.5% - 2% on committed capital during the investment period (i.e. including during the period before any capital is drawn down and investments are made) and on invested capital thereafter.

Founders' incentive structure

Typical SPAC	Typical Private Equity Fund
For NASDAQ listings: A 'promote' - typically 20% of the post-IPO equity - issued to the founders upfront for nominal consideration. The promote is an outright ownership position (unlike carried interest, which is a % of profits) and not subject to a priority preferred return/hurdle for investors. For LSE main market listings: The 'promote' is typically structured as: (i) a preferred annual dividend (payable in ordinary shares or cash) or other 'enhanced rights' on the founders' preferred shares which in substance give the founders a priority return (typically 20%) of the increase in the market value of the ordinary shares, once a business combination has been consummated and the market value of the ordinary shares has hit a specified hurdle (typically $11.50 / 115% of the initial issue price of $10.00), and subject to a high watermark provision; together with (ii) a preferential return (typically 20%) of any dividends otherwise payable on the ordinary shares.	Varies widely but often 15% - 30% of profits subject to a priority preferred return/hurdle (often approximately 8% - 10% IRR) for investors.

Organisational / formation costs and expenses

Typical SPAC	Typical Private Equity Fund
Typically fronted by the founders and/or paid from interest earned on the escrow account. Founders are 'at risk' for this if a business combination is not ultimately consummated.	Paid by the fund from investors' capital (often subject to a maximum expenses cap).

Transparency

Typical SPAC	Typical Private Equity Fund
Public company transparency.	Limited transparency – prescribed investor reporting regime (subject to investor side letters).

Investor side letters

Typical SPAC	Typical Private Equity Fund
No.	Yes.

Investor base

Typical SPAC	Typical Private Equity Fund
Typically comprised of institutional investors and hedge funds, although no investor qualification requirements apply.	Various investor qualification requirements apply as well as significant minimum capital commitments (which, combined, effectively exclude non-professional and unsophisticated investors).

Liquidity / exit

Typical SPAC	Typical Private Equity Fund
Investors can sell their shares and/or warrants in the open market. For NASDAQ listings: Further ability for investors to withdraw capital (their pro rata share of the balance of the escrow account) in the following circumstances: • a shareholder vote to approve a proposed business combination transaction or a tender offer in connection therewith (discussed above); or • failure to consummate a business combination within the permitted investment period. The escrow account provides downside protection in the form of a minimum liquidation valueper share.	Very limited liquidity. General partner consent required for transfers (subject to exceptions for permitted transfers to affiliates etc.) and distributions at sole discretion of general partner of the fund.

The Popularity of the BVI for SPACs

The BVI is one of the most popular jurisdictions for incorporating a SPAC. The key reasons for this are:

Best in class company law

BVI has progressive, flexible and business-friendly company law legislation, often considered an anglicised version of Delaware company law and supported by English common law precedent and analysis. In particular:

- There is a high degree of flexibility to tailor bespoke governance and capital arrangements (including equity warrant and redemption provisions, the efficient functioning of which are critical to SPAC structures) and to adapt to applicable onshore listing rules and investor preferences (as considered appropriate).
- There is a high degree of flexibility to tailor dual or multi-class investor voting rights, to mitigate the risk of 'no votes' blocking proposed business combination transactions.
- BVI companies may have unlimited purposes/objects, which is important for SPACs with broad investment mandates.
- The BVI has an efficient statutory merger regime (modelled on Delaware law) conducive to SPAC business combination transactions.
- There are no mandatory investor pre-emption rights and few mandatory minority shareholder protection rights – the vast majority of corporate actions and decisions may be made by the directors without further approval by shareholders.
- There is no requirement for BVI-resident directors.
- There is no mandatory concept of share capital/premium or capital maintenance (thereby avoiding the attendant cumbersome rules and restrictions regarding par value and share capital). Shares may be redeemed quickly and with minimal administrative hassle (the only requirement for distributions being satisfaction of a cash flow and balance sheet insolvency test).
- There is no BVI takeover code or equivalent or any specific statutory provisions which apply to listed BVI companies – meaning a BVI company can elect to adapt and adhere to onshore codes and rules without the risk of 'double legislation'.

U.S. FPI status

With appropriate structuring, a BVI company listed on a U.S. exchange may be eligible to qualify as a 'foreign private issuer', thereby potentially benefiting from relaxed U.S. regulatory requirements and certain concessions (as compared to U.S. domestic issuers) regarding regulatory filings (quarterly financial reports not required), proxy solicitations (filings with SEC not required), audit committee requirements, and disclosure requirements regarding executive compensation and equity holdings of directors and officers.

Ease of leveraged financing

BVI has a straightforward and effective system for registration of security interests granted by a BVI company. This, when combined with a sophisticated insolvency regime which is perceived to be friendly to secured creditors, facilitates the leveraged financing a SPAC may require to consummate a business combination transaction.

Sophisticated and reliable judicial system

BVI has a dedicated and experienced Commercial Court, with ultimate appeal to the Privy Council of the United Kingdom.

Global recognition and familiarity

BVI companies and company law are recognised by and familiar to sophisticated investors, lenders and securities regulators worldwide.

Cost efficiency and ease of incorporation

BVI companies are comparatively inexpensive to form and maintain, and can be incorporated very quickly (on a same-day basis, if necessary).

Tax neutrality

No taxes or duties are assessable in the BVI on a BVI company or its international investors. Taxes may of course be assessed onshore in the ordinary course against the BVI company (e.g. in those jurisdictions where the company's assets, operations or business are based or conducted) and its investors (e.g. in those jurisdictions in which the investors are tax resident or otherwise liable to pay tax).

International compliance

BVI adheres to all applicable international compliance standards. BVI is listed on the OECD's 'white list', is a member of the International Organization of Securities Commissions (IOSCO) and is FATF compliant.

Strong track record and ease of execution

Having raised more than US$5 billion over the past 7 years, BVI SPACs have a strong track record and are familiar to both investors and regulators. The legal structure of SPACs tends to be relatively similar between deals making execution of a successful transaction easier and more efficient.

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