Proposed TSX Amendments to the SPAC Regime

July 16, 2018

On June 1, 2018, the Toronto Stock Exchange (the "TSX") requested comments on proposed amendments to the TSX company manual relating to special purpose acquisition corporations ("SPACs"). The proposed amendments are intended to codify certain standard exemptive relief granted in connection with SPACs and to address challenges with the SPAC regime. The proposed amendments will become effective following the completion of the public notice and comment and approval by the OSC. Comments were to have been provided to the TSX by July 3, 2018.

Background

SPACs are an alternative investment vehicle for private issuers looking to list on the TSX and provide members of the public with a vehicle to invest in companies or industry sectors normally sought by private equity firms. At a high level, SPACs are formed by a small group of seasoned directors and officers (usually sophisticated financiers and managers) and are listed on the TSX via an initial public offering raising a minimum of C$30 million. Ninety per cent of the funds raised in the IPO must be placed in escrow, and must then be used toward the acquisition of one or more operating companies or assets within 36 months of listing.

An Inauspicious Start

SPACs grew in popularity in the United States immediately prior to the financial crisis of 2008/2009 and were introduced into Canada in December 2008. SPACs were seen as providing the public with the opportunity to co-invest with sophisticated financial players in opportunities that would normally be restricted to private equity firms and institutional investors. They also provided certain other benefits including: (i) flexibility in accessing capital for new opportunities, (ii) removing the potential for integration issues incumbent with strategic buyers, (iii) an efficient means of becoming a public company, and (iv) the ability to provide target shareholders with liquid shares rather than cash consideration (thereby allowing for certain tax efficiencies).

However, despite the many benefits associated with SPACs, they have struggled to take hold in Canada as a viable investment vehicle. Since the inception of the TSX SPAC regime, only six SPACs have been launched in Canada of which four have

completed successful qualifying transactions. One of them, Acasta Enterprises Inc., has recently announced it is in “serious financial difficulty” and has since sold two of its three operating businesses. This lacklustre start has led many commentators to point out various factors militating against the success of SPACs in Canada, particularly vis-à-vis their relative success in the United States:

- there are fewer large deals in Canada, meaning SPACs are competing with established investment funds and private equity funds for deals;
- smaller deals involving early stage companies are typical in Canada and usually involve longer investment horizons before returns can be realized, making them less attractive for SPAC investors;
- to date, investors have typically been hedge funds who have used their voting power to hinder transactions which they do not find attractive; and
- despite the efforts to make SPACs a more efficient mechanism for private entities to go public, they still remain very costly and time consuming, particularly as the initial founders are liable for the costs associated with the IPO, maintaining the SPAC and the qualifying acquisition.

We also note that the TSX Venture Exchange’s immensely successful Capital Pool Company Program is well entrenched and has served participants well in small and mid-cap going public transactions.

Proposed Amendments

In developing the proposed amendments, the TSX met with various industry stakeholders including founders, dealers, lawyers and investors involved with the SPAC regime in order to gather feedback and address existing challenges. The proposed amendments would, among other things, provide for the following:

1. Revise the current redemption rules to limit the maximum exercise of redemption rights by any shareholder provided that the limit is not below 15 per cent of the shares sold in the IPO. This amendment may address the issue that SPACs have had with ensuring certainty of capital when pursuing a qualifying transaction given that large numbers of shareholders typically seek to redeem their securities (in some instances over 95 per cent).
2. Permit founders to provide loans to the SPAC, provided that the loans are without recourse to the escrowed funds, the principal amounts are limited, the details are publicly disclosed, and the loans are commercially reasonable. This will provide SPACs with additional flexibility to fund ongoing operations and expenses, and to identify potential targets for a qualifying acquisition.
3. Remove the requirement that SPACs hold an annual meeting and provide public shareholders notice and an opportunity to speak. Given that SPACs do not have an operating business (aside from identifying potential acquisition targets), and that public shareholders do not have voting shares, this amendment is intended to reduce administrative burden and reflects existing exemptive relief granted by the TSX.
4. Remove the requirement to obtain shareholder approval for a qualifying acquisition provided that at least 100 per cent of the gross proceeds raised in the IPO are placed in escrow, a notice of redemption is mailed to shareholders, the prospectus is posted on the SPAC’s website and the SPAC delivers a copy of the

prospectus to investors. It is hoped that this amendment will accelerate the timelines to close qualifying acquisitions.

5. Reduce the public distribution requirements from a minimum of 300 public board lot holders to 150. This should make the IPO that much more efficient by reducing the number of smaller, retail shareholders required to participate.

It is hoped the proposed amendments will serve to jump-start the SPAC regime as a viable mechanism for both investors looking to acquire privately held operating companies, and for private companies looking to list on the TSX in an efficient manner. Should you have any questions or would like further information about these developments, please contact a member of our Securities and Capital Markets Group.

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