

SPACS AS AN INSTRUMENT OF BENEFICIAL CHANGE IN CORPORATE GOVERNANCE, AIMED AT COMPANY GROWTH: THE FIRST ITALIAN INSURTECH-BASED INSURANCE COMPANY

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Abstract

The paper begins with the definition of the concept of SPAC ("Special Purpose Acquisition Companies"), as a corporate vehicles constituted with the objective to carry out - after raising capital - an investment in one or more existing operating companies ("target company"). We focus on the peculiar aspects of the SPAC as an instrument of beneficial change in corporate governance, aimed at company growth. Therefore, a summary picture of the situation of the SPACs in the Italian context is provided, proceeding, finally, to the analysis of the case of NET SPA, the first insurtech based Italian insurance company, created through the SPAC tool.

1. INTRODUCTION

"Special Purpose Acquisition Companies" ("SPAC") are corporate vehicles constituted by one or more promoters in view of the listing ("IPO") on a regulated market or on a multilateral trading system (AIM Italia), with

the objective to carry out – after raising capital through the IPO of the SPAC - an investment (generally through the acquisition of investments and/or a merger) in one or more existing operating companies ("target companies").

SPACs draw origin from the "blank check companies", company that started to operate on the US market at the beginning of eighties and defined by Securities and Exchange Commission (SEC) "a development stage company that has no specific business plan, or purpose, or has its business plan to engage in a merger or acquisition with an unidentified company, other entity, or person"¹.

After a first period, in which the regulation of blanks check companies was simplified compared to that of larger listed companies (blanks check companies issued the cc.dd. " Penny stocks" and were operating on the "penny stock market "), at the beginning of the nineties SEC introduced a more stringent discipline on the placement of blank check companies securities, providing for the application of "Securities Enforcement Remedies and Penny Stock Reform Act" of 1990 and of "Rule 419"(from which the characteristic features of modern SPACs are derived)².

As mentioned, "SPAC" refers to companies established by one or more sponsors, who provide the initial capital needed to finance the operational management and current expenses of the SPAC up to its listing.

After the establishment of the SPAC, the sponsors approve a capital increase to serve the company's listing, aimed at providing the company with the resources necessary to make an investment, within a certain maximum term (generally in the following 18/24 months), in a target company not yet identified at the time of the IPO³.

The "special purpose" of the SPAC consists, therefore, in the research and acquisition of an unlisted target company – which presents significant growth prospects – whose identification is delegated to the promoters of the SPAC. The latter are typically subjects with recognized entrepreneurial and managerial skills as well as scouting skills in the sector, able to boast an extensive network of contacts or professionals with a solid track record in M&A and private equity.⁴

¹ Chiomenti, C. & Graffi, L. (2010). La "Special Purpose Acquisition Company". *Giurisprudenza Commerciale*, 1, 445-450.

Shachmurove, Y., & Vulcanovic, M. (2017). SPAC IPOs. In D. Cumming, & S. Johan (Eds.), *Oxford handbook of IPOs*. Retrieved from www.ssrn.com.

Murray, J. S. (2017). Innovation, limitation and regulation in finance: The evolution of special purpose acquisition corporation. *Review of Integrative Business and Economics Research*, 6(2), 1-27. Retrieved from www.ssrn.com.

² Rule 419 already required, inter alia, a maximum period for the investment (eighteen or twenty-four months), rigid limits on the use of liquidity by promoters, the shareholders' investment requirement with majorities particularly qualified (eg 80% of the share capital), the right of withdrawal in the event of failure to obtain authorization.

³ Donativi, C., & Corigliano, P. (2010). SPAC (Special Purpose Acquisition Companies): The international model and its compatibility with Italian law. *Società*, 17.

⁴ Barcelona, E. (2018). *The "collective management of savings" following the AIFM Directive. Investment companies, family offices, club deals, SPAC, holding companies*. Milan: Giuffrè.

SPAC promoters do not receive a predetermined remuneration for the work performed, nor – unlike the managers of a private equity fund – a fixed commission calculated on the mass of the managed capital (so-called “management fee”) but are remunerated only at the time of the business combination, through warrants to subscribe ordinary shares on particularly advantageous terms, or special shares, with reward conversion ratios. If the transaction is not carried out within the set deadline, the promoters do not receive compensation and the paid-up capital is returned pro-rata among the shareholders.

Once the promoters have identified a target company, that presents the characteristics indicated in the "investment policy" adopted by the SPAC, they submit the transaction to the approval of the shareholders' meeting with full disclosure of the characteristics of the target company, including the information relating to the business of the latter and to the specific sector in which it operates. This allows investors to control the ways in which the money invested is used by the managers of a SPAC, thus mitigating one of the main risks inherent in the investment, and specifically "the impossibility for a potential investor to rely on past returns of the company"(track record)⁵.

Shareholders of a SPAC can vote for or against the completion of the business combination, with the clarification that those who have not participated in the adoption of the decision will have the right of withdrawal.

Usually, shareholders' meeting of a SPAC resolves on matters reserved to it with the majorities provided by the law, depending on whether or not it can be classified as a company that makes use of the risk capital market (pursuant article 2325-bis civil code), it being understood that it is common for the articles of association to condition the effectiveness of the resolutions functional to the implementation of the business combination to the failure to exercise the right of withdrawal and repayment in excess of a predetermined threshold.

The investment in target company can be made in different ways, although market practice has shown that target company is usually incorporated by the SPAC, with the result that the acquired company - which was previously a "closed" company – automatically achieves the status of a listed company; it is however possible that the target company incorporates the SPAC, with the consequence that SPAC shareholders will receive in exchange shares of target company (which, in the meantime, will have started and completed the listing process so that, at the time of the effectiveness of the merger, SPAC shareholders can receive quoted shares of the target without interruption). It could also happen that the SPAC limits itself to acquiring social participation in the target company without proceeding to further company integration; so that SPAC takes the form of a holding company.

⁵ See Chiomenti, C. & Graffi, L., *op. cit.*

As mentioned, it may happen that upon expiry of the duration of the company it was not possible to complete the business combination: in this case, SPAC is put into liquidation.

In summary, in light of the above, we can say that the main advantages of SPACs are:

- *the centrality of the investor*: the investor is at the center of the decision-making system, the decision of the Business Combination is always delegated to the shareholders, with the possibility of exit for the individual dissenting shareholders;
- *presence of an experienced and motivated team*: investor can make use, in fact, of the ability of a management expert in the selection and acquisition of unlisted companies, often on better terms than the possibilities offered by the market of listed companies and the remuneration of the management is largely linked to the performance of the post Business Combination title.
- *liquidity of the investment*: the ordinary shares and warrants of the SPAC are negotiated separately on the stock market from the beginning and the investment can be converted from the first day of listing. Furthermore, the warrants allow the investor to generate a minimum return or to realize an additional upside on the investment.
- *downside protection*: the effective implementation of the Business Combination is subject to the prior approval of the Shareholders' Meeting. Members who have not participated in the approval of the change in the corporate purpose (necessary to complete the Business Combination) may exercise the right of withdrawal. Furthermore, as has already been pointed out, if the Business Combination is not approved within the maximum term of the SPAC, the SPAC will be dissolved for the duration of the term and will be placed in liquidation

2. SPACs: A SHORT LITERATURE REVIEW

SPAC literature is quite fragmented and scarce considering the European SPACs.

Obviously this is due to the fact that, as already specified above, this type of instrument began to spread first overseas and, only a few years ago, also in Europe.

Most of the contributions concern the development of the SPAC in the American market, comparing it with the current US legislation; only since 2013 were published the results of a research conducted on a sample of European SPACs published.

The first studies on the subject analyzed the legal and accounting profiles of the SPACs, highlighting the characteristics of this type of instruments and studying their compatibility with legal regulations (always with reference to the American context). The subsequent empirical work also focuses on a particular aspect of operations (returns,

price trends, comparison with private equity investments or with respect to IPOs, etc.).

The main contributions made on the SPAC would include Hale (2007), who summarized the main features of the SPACs, retracing the life cycle of these companies and commenting on the salient aspects of the transaction (the composition of the investors, the segregation of funds raised, the approval of the business combination, the distribution of warrants to promoters, etc.).

The conclusion it reaches is that the SPAC is a tool that has advantages for all those involved (promoters, investors and target companies).

In 2008, Berger notes that the emergence of the SPAC phenomenon represents a strategic option for companies that want to access the capital market without going through the traditional IPO. Analyzing only a few success stories, it highlights the advantages and disadvantages of this process.

Davidoff and Sjostrom (2008) analyze the SPAC from a legal point of view; the first in the field of the regulation of retail investments in risky operations (in hedge funds, private equity, etc.) and the second trying to catch the differences between the SPAC and the other blank check companies.

In regards to the empirical analyzes on the subject, we would mention Jog & Sun (2007) who studied

a sample of 62 SPACs between 2003 and 2006, compares the returns obtained by investors and founding members.

Boyer & Baigent (2008), reported the results of a research on a sample of 87 American SPACs from 2003 to 2006, the year in which the phenomenon reached significant dimensions with more than 3 billion dollars collected.

Jenkinson & Sousa (2009) analyzed a sample of 43 American SPACs, trying to give a meaning to price fluctuations after the date of announcement of the business combination.

Rodrigues and Stegemoller (2011) made a comparison between SPAC and private equity, in terms of financial contracting, trying to highlight the substantial differences.

Datar et al. (2012) developed an interesting comparison between a sample of 156 SPACs and 794 traditional IPOs to try to catch the differences between the target companies and those that choose the listing route. The sample refers to the 2003-2008 period and analyzes operational performance (adjusted for sector results) and share returns in the first year of life as listed companies. Operating performance analyzes the dimensions (in terms of total assets, capitalization and revenues), profitability (EBITDA, operating flows, ROA), solvency (liquidity index, debt ratio, interest rate coverage), expenses for investments and growth opportunities (P / E, P / sales, Market value / Book value).

Cumming et al. (2012) analyzed which factors influence the approval of the business combination, finding the composition and type of

investors to be significant in this regard. The probability that it will be approved is reduced with the increase in the presence of hedge funds and private equity funds, while it is easier when the promoters / directors have a significant amount of shares.

Ignatyeva et al. (2013) published the first research on European SPACs and includes a sample of 19 cases concluded between 2005 and 2011. Of these, two were liquidated and 17 were successfully completed (including the first SPAC with an Italian target). The analysis shows that the European SPACs have an average size of 489.4 million euros, much larger than the American ones (210.8 million according to Datar et al., 2012) but with a median of 275 million which indicates that in half of the cases they take on more limited dimensions (on the average there are two particularly large collections).

In a recent Italian study by Fumagalli (2014), the focus is on the development of SPACs in Italy as a new way of doing private equity and listing companies on the stock exchange.

3. SOME DATA ON SPACS IN ITALY

In Italy, SPACs are governed by the regulation of the markets organized and managed by Borsa Italiana SpA (the "Market Regulations") and referred to the type of "companies established for the purpose of acquiring a business whose exclusive corporate purpose includes investment predominantly in a company or business, as well as the related instrumental activities "or those" whose investment strategy has not yet been started or completed and / or is characterized in terms of particular complexity "⁶.

Shares of a SPAC can be traded on the professional segment of the MIV market ("Electronic Investment Market vehicles") or on the multilateral trading system AIM Italia (Alternative Capital Market), in which they are defined as "companies established for the purpose of acquiring a specific business and included in the category of" investment companies".

Since 2011, SPACs and vehicles substantially similar to SPACs have collected just under 4 billion euros and have invested a total of over 2 billion euros, still having a figure of just under 2 billion.

Six companies were listed on the Italian Stock Exchange in 2018: Industrie Chimiche Forestali (May), Cellular Italia (June), CFT (July), Guala Closures (August), Fine Foods Pharmaceuticals (October) and Digital Value (November).

The first months of 2019 have already seen the integration between the Interprovincial Bank and the SPAC Spaxs that gave birth to Illimity, as well as the merger between SPAC Gear 1 and Comer Industries which was listed on AIM Italia on March 13, 2019.

⁶ This is essentially the definition of "SIV", contained in the previous versions of the Market Regulation (until 25 June 2018).

SPACs are therefore a useful tool to encourage SMEs to access the capital market, to accelerate their growth also in the international arena.

4. NET INSURANCE: THE FIRST ITALIAN INSURTECH BASED COMPANY

For the first time in Italy, SPAC tool was used to build an insurtech based insurance company.

More specifically, the SPAC Archimede and the target company Net Insurance (the company that has built over the years a high competence in insurance coverage of fifth-place divestment products) has given rise to a new business combination model desired by many.

Business plan 2019/2023⁷ provides that, relying on the specific managerial and entrepreneurial track record of the promoter and management team, it will generate a number of positive effects linked together and namely:

- the strengthening and profitable growth of the company that will be born with the business combination;
- an independent non-life bancassurance platform;
- a distinctive service capacity to the insurance distribution networks;
- full use of Insurtech innovation in all business processes.⁸

Going into more detail about the NET Business Model, we can explain how its Mission is to “build an open B2B2C platform, independent and specialized in the business of protecting people and their assets, enhancing all the innovation opportunities offered by digital technologies.”

Mission Strategic Pillar are, therefore:

- the enhancement of the salary-backed business;
- the development of non-life and protection bancassurance;
- the development of the non-life retail broker channel;
- digital platforms.

Furthermore, some "transversal enabling factors" of the business model have been identified and namely:

1. high capitalization;
2. the adoption of a new organizational structure with the enhancement of middle-management;
3. a technology architecture focused on high value-added strategic assets and which includes:
 - a sales front end to optimize the integration with partners and the effectiveness of the placement;
 - a data hub to extract the maximum value from the potential wealth of the data;

⁷ Net Insurance Spa (2013-2019). *Business plan presented, to the Italian Stock Exchange on June 19, 2019*. Retrieved from www.netinsurance.it.

⁸ For the target company, the merger represents a strengthening of the social capital and a change in governance, preparatory to consolidate company's relaunch with the planned increase in turnover volumes and profits. According to the SPAC estimates, after the merger, target company will significantly exceed 200% of solvency ratio.

- cyber security as a transversal layer to reduce IT risk;
 - the creation of partnerships for innovation with insurtech companies.
4. strong focus on brand equity through:
- sponsorship of Italian football referees;
 - development of a range of specific products for the football world network;
 - implementation of activities to support relations with the various stakeholders.

In summary, the business model, its strategic pillars and transversal enabling factors are declined in five business areas (the sources of value):

- the divestment of the fifth;
- bancassurance;
- the broker channel;
- digital and insurtech platforms;
- financial investments.

5. CONCLUSION

The success achieved by SPAC in the Italian markets is due to the appeal that this model has registered with investors and entrepreneurs/targets.

With reference to investors, the characteristics of the SPAC that have made this form of investment particularly appreciated are mainly the following:

- the investment has a relatively low risk profile, since, in the event of failure of the planned initiative, the investors obtain reimbursement of the initial investment (with a minimum remuneration represented by investments made against the escrow account with which the SPAC had deposited the capital collected during the IPO);
- each investor (as shareholder of the SPAC) may withdraw from the SPAC following the meeting convened for the business combination (receiving back, even in this case, the capital invested with the accrued income);
- the valuation and acquisition of the target company is usually carried out "at a discount" with respect to market values, and therefore SPAC investors – immediately after the business combination with the target company - could immediately benefit from a potential appreciation of the shares listed companies of the target company.

In the perspective of the entrepreneur who owns the target company, the SPAC has the advantage of accelerating the listing process of the target company and, at the same time, mitigating the risk that, at the time of fixing the offer price for the IPO (of the target company), the market conditions (in terms of valuation, volatility, etc.) do not allow a sufficient appreciation of the stock quoted.

Otherwise, using the SPAC scheme, the valorisation of the target company (in terms of exchange ratios, etc.) is established independently by the parties regardless of market conditions (avoiding the "book building" mechanism).

These elements have made SPAC one of the most appreciated forms of investment in current market conditions, which compete with more traditional ones.

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