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Failed SPACs Popular Investments

Shareholders Push for Early Liquidations to Tap Trust Cash

by Mark Mueller

The management teams of many – if not most – SPACs still on the lookout for a suitable target company are dealing with an unpleasant fact.

A large percentage of their shareholders, especially investors who've bought common stock in the past quarter or so, aren't looking for a merger to be announced, let alone completed.

And they'd prefer their SPAC to wind up operations and liquidate as soon as possible, thank you very much.

New investors are, by and large, just looking at a SPAC's internal rate of return, based on its stock price and the value of its money held in trust. And they're also assuming the SPAC will liquidate without making a deal, said David Miller, managing partner of New York-based law firm **Graubard Miller.** Many investors in SPACs today "just want the trust dollars," he said.

These stockholders have emerged as hedge funds, traditionally the cornerstone of SPACs' investor base, continue to sell off portions of their assets at a loss to raise cash for investor redemptions.

A few months ago, SPACs had been trading at discounts of 10% or more compared to the money they've raised in initial public offerings. That gap has closed slightly but, in many cases, these blank check companies are still trading at significant discounts.

Privately held funds are raising cash to buy discounted SPACs. Retail investors and high net-worth individuals are also buying into the SPAC market, which is being promoted as a safe short-term investment backed by U.S. Treasuries.

"If you're SPAC management, you have to assume that those investors will vote no for any deal, regardless of its qualifications," Miller said.

The management teams of a few companies appear to have taken the hint.

Churchill Ventures, a $108 million SPAC, said in November that it would suspend its search for an acquisition target and likely liquidate, nearly three months ahead of its 24-month deadline. A shareholder vote on the liquidation plan is set for later this month.

"We would rather close our doors and return our investors' capital than pursue a business combination in these market conditions," Churchill chief executive Christopher Bogart said in a statement.

The SPAC, which went public in March 2007 at $8 per share, said that it reserved its right to call off the liquidation if it does happen to come across a suitable transaction in the meantime.

"Churchill's founders will lose money personally by taking this decision – and our shareholders will actually turn a profit on their investment in Churchill – but we believe strongly that it is the right thing to do rather than bringing a questionable transaction to the market," Bogart said.

Shareholders in Churchill will receive about $8.15 for each share they hold.

Question of Time

Short-term investors are likely hoping that other SPACs will follow Churchill's lead. They've been pouring money into discounted SPACs the past quarter, with little thought about the liquidation provisions of each specific company. That could turn out to be a mistake, some in the industry suggest.

"Investors may not necessarily get back their money when they think they will," said one underwriter of numerous SPAC deals. The particulars of every SPAC's trust investment need to be understood before making an investment, he said.

To be sure, there's never been a SPAC that's liquidated which hasn't returned its IPO funds held in trust back to investors.

"Are people getting their money back? Yes. The question is if they're getting it back in a timely fashion. Some have taken longer than expected," said Barry Grossman of New York-based law firm **Ellenoff Grossman & Schole.**

The liquidation of **Affinity Media International Corp.,** a $19 million SPAC, went several months beyond what was anticipated.

Affinity was expected to dissolve in June after failing to complete a roughly $29 million acquisition of **Hotels At Home,** a publisher of retail catalogues marketed to hotel guests.

Rather than immediately liquidating, Affinity asked its shareholders to approve a measure that would allow the company to continue after its liquidation as a shell company. That request was approved in October.

Deals like Affinity's are expected to become less likely going forward.

Beginning in late 2006, most SPACs chartered in Delaware began including streamlined, automatic liquidation provisions, which mandate that the SPACs dissolve if deals aren't reached within a specific period of time, typically 24 months.

The provision for a so-called "exploding charter" have become more popular for SPACs coming to market since then, although not all blank checks reaching their due date late this year and in early 2009 have the provision.

"With a limited life charter, the only thing you're allowed to do [at a certain point] is dissolve," said Miller. "If you're an investor, it gives you a sense of assurance as to the timing of your liquidation payment."

Older SPACs that don't have the exploding charter provision can continue their corporate existence as shell companies with shareholder approval. That's a big "if", though, especially since its likely to add time and other complications to the liquidation process, notes Grossman.

There's also talk in the industry that at least one SPAC with an exploding charter might be looking to amend the charter, to keep the company viable beyond its two-year lifecycle, Grossman said.

If a SPAC doesn't include a limited life charter, delays could turn a can't-miss short-term investment into something more complicated. Proxy votes, SEC approvals and other complications can add months onto the time when investors get their money back.

Foreign-based SPACs, such as those operating under Cayman Islands law, usually offer liquidation provisions that provide greater leeway than in Delaware-based SPACs, and are seen as more likely to delay liquidation.

Some big investors in the SPAC market have used the specter of law-suits to keep liquidation delays at a minimum.

In October, hedge fund **Bulldog Investors** filed a petition in a Delaware court to compel SPAC **Dekania Corp.** to liquidate, a few weeks after shareholders of its merger target, **Advanced Equities Financial Corp.,** rejected the planned combination.

In the case of Dekania, Bulldog said it didn't believe the SPAC could complete a deal with Advanced Equities, or another company, in the time the SPAC has left under its charter. Dekania would only have until February to find and acquire another company.

In mid-November, Bulldog and Dekania agreed, among other things, to cancel a hearing on the petition, and to hold an annual stockholders meeting by early February. The meeting will include discussion of a liquidation plan, the company said.

Bulldog Investors and its affiliates own about 7.4% of Dekania's outstanding shares, according to recent ownership filings.

Nearly a quarter of the activist investor's holdings in the SPAC, which raised about $100 million in its IPO, were acquired after Advanced Equities shareholders nixed the proposed merger. Besides Dekania, Bulldog is said to have used similar threats of lawsuits to speed up the liquidation plans of at least one other SPAC, according to industry watchers.

Too Soon?

Rather than taking too long to liquidate, Grossman notes that the big issue going forward could be from SPACs, such as Churchill, that decide to close up shop well before its 24-month life cycle is complete.

If a SPAC opted to liquidate at month 23, with only a few weeks left, there likely wouldn't be much opposition. But warrant holders of a SPAC that wanted to liquidate a few months earlier could try to challenge such a move in an attempt to salvage something from warrants that would be rendered useless.

Miller believes a challenge from warrant holders is unlikely since management has no fiduciary duty to them.

"Say you're in month 21 or 22, and know that you can't get a deal closed. The question is: Do you decide to give the money back that day? It's a difficult issue. I can see either side [of the argument]," Grossman said.

Along with Churchill, **Transforma Acquisition Corp.,** a $100 million SPAC, is among the most recent blank check firms to close shop a little earlier than expected.

The company said in late November it planned to liquidate because it would not be able to complete a business combination by its Dec. 26 deadline. A shareholder meeting on Dec. 22 is planned.

While other management teams looking to close deals in the next few months could consider early liquidations, it isn't a given that 2009 will be remembered just for SPAC liquidations, rather than completed mergers, some say.

There's a silver lining to the tumult on Wall Street, Miller said. "What's positive for the industry is that the longer the period of market and economic uncertainty goes on, the more precious a SPAC with a boatload of cash in trust becomes," he says.

Private companies looking to go public will continue to be shut out of private equity and hedge funds, as well as venture capital. That will give SPAC management teams who have enough time to get a deal done a larger base of target companies to choose from.

"A SPAC with the time to get a deal done should be pretty optimistic right now because other sources of capital have completely dried up," Miller said.

But even so, to get a deal done, a company's management team "needs a damn good target, at a damn good valuation," he added.

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