POTENTIAL BEYOND BOUNDARIES TIMES ASCENT

Publication: Economic Times Mumbai; Date:2008 Jun 04; Section:Markets; Page Number 14

What's special about special purpose acquisition vehicles?

Abir Roy & Vyapak Desai

THERE are numerous kinds of investment vehicles that are prevalent, most notably being private equity funds and venture capital funds. One of the most emerging types of investment vehicles that is surfacing in recent times are Special Purpose Acquisition Companies (SPAC). SPAC is a company which has nil or minimal operating business and assets and proposes to launch an initial public offering (IPO) in order to raise capital from the public for effecting a merger, asset acquisition or other forms of business combination. Thereby, SPAC are also referred to as 'blank cheque' companies. The USP of having a SPAC over other forms of investment vehicles is the inbuilt mechanics of investor safeguards that are ubiquitous in the working of SPAC.

Recently, the founders of the UK-listed investment firm Promethean raised a $200-million SPAC called Atlas Acquisition Holdings in the US, the largest-ever SPAC targeted prominently at India. There are around 66 SPACs that currently filed with Securities and Exchange Commission (SEC) and 21 from 2008. This article analyses the spectrum and modus operandi of SPAC.

It has been a prevalent market practice that the target company must have a fair market value equivalent to a minimum of 80% of the net assets of the SPAC at the time of acquisition. Unlike in a private equity fund, when a SPAC proposes to enter into an acquisition or a business combination, the same should be approved by majority of the shareholders/investors of the SPAC. Subsequent to entering into a definitive agreement for venturing into a business combination, a statement or notice is issued to the shareholders of SPAC, disclosing the material particulars of the transaction including completed audited financial statements of a target company.

There are numerous investor safeguards that are in-built into the modus operandi of SPAC, which include:

• The shareholders have a right to vote on the transactions that a SPAC wishes to enter into. The majority of the shareholders should vote in favour of the proposed business combination and there is normally a requirement that not more than 20% of the shareholders should exercise their conversion rights or sell the shares held by them in the open market.

• The various options available to a stockholder in a SPAC who wishes to vote against the business combination are:

• The shareholders have an option to sell the shares held by them in the open market since a SPAC trades on the exchanges unlike investors in a private equity fund who are locked in for a period of time.

• The shareholders can exercise their conversion rights wherein the shareholders are entitled to convert the warrants held by them into pro rata share of the trust account.

• Further, in the event that the SPAC cannot initiate or consummate a business combination within a particular timeframe, the SPAC shall be liquidated and the trust account will be released to all the shareholders. The management of SPAC is required to deposit the shares held by them prior to the IPO into an escrow account to be maintained by the underwriter. This account is not transferable during the escrow period. In such an event, the management would not participate in the distribution occurring upon liquidation for the escrow shares. However, the management has the right to vote on the transactions with respect to such shares and receive dividends and other economic rights.

• The SPAC is led by people who are experts in acquisition.

• SPAC will have adequate corporate governance norms as it is a public listed company.

It would be interesting to see how the regulatory authorities react or respond to listing of SPACs in India through IPO process. Since, SPAC is normally a “shell” company which raises proceeds through an IPO, it may be difficult for a SPAC to satisfy certain eligibility norms and disclosure requirements as prescribed under the Listing Agreement and Sebi Guidelines, for example, profitability track record. However, it may still be possible for a SPAC to consummate an IPO by fulfilling certain alternative eligibility criteria.

(The authors work for the law firm Nishith Desai Associates)


RAJESH KARANDE