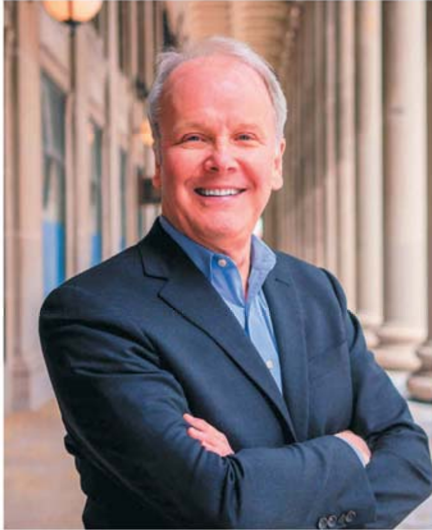

Surveying SPACs: A Skeptic's Stance

Special purpose acquisition companies are raising record amounts of capital, but are they worthwhile investments?

Mark J. Gilbert, CPA/PFS, MBA
President, Reason Financial Advisors
mgilbert@reasonfinancial.com
ICPAS member since 1982

As accountants and advisors, many of us know of successful private companies run by exceptionally intelligent leaders. Perhaps some of us would love to invest in them, or in other equally successful private companies. After all, the market for investable public companies is small compared to the private company market: According to the World Bank, there were 4,266 publicly traded companies in the United States at the end of 2019. At the same time, there were, at least by one estimate, about 7.5 million privately held companies. That's a ratio of at least 1,700-to-1. Not all private companies are worth investing in, of course, but doesn't it seem that the private company market is an untapped investment opportunity? After all, angel investors, venture capitalists, and hedge funds invest in private companies—why can't the rest of us? Special purpose acquisition companies (SPACs) are a way to do just that.

SPACs are publicly traded corporations which have been set up for the purpose of taking privately held companies public without going through the traditional initial public offering (IPO) process, thus simplifying the process. These corporations raise funds from investors based merely on the sponsor's intent to find a great company to invest in. SPACs will often identify a target industry or some other area of focus—technology, electric vehicles, and renewable energy companies have recently been attractive targets for SPACs. SPACs are typically short-lived, as they're generally required to invest the funds they've raised within a period of 18-24 months after launch or return them to their investors.

While SPACs have been around since 1993, they used to be regarded as a less desirable method for a privately held business to go public than the traditional IPO process. However, the rising costs of traditional IPOs, coupled with the interest of wealthy entrepreneurs to personally diversify their own investments, has led to increasing enthusiasm for SPACs over the past two years. According to the Wall Street Journal, SPACs raised $83 billion in 2020, which exceeded the combined amount raised in all prior years. In the first quarter of 2021 alone, SPACs raised about $100 billion. By the end of the first quarter of 2021, there were approximately 400 funded SPACs looking for privately held businesses to acquire.

But SPACs may start experiencing some growing pains as their tremendous growth rate has attracted greater levels of scrutiny. In April, the SEC released a statement requiring that the warrants which SPACs create and distribute to their initial investors be treated as a liability rather than equity, thus increasing their expenses and weakening their

financial positions. Only time will tell whether this accounting issue will negatively impact the continued viability of SPACs as a vehicle for taking businesses public.

So, are SPACs worth investing in? As SPACs hold a host of companies in a variety of industries, it can be difficult to draw an unqualified conclusion. Lumping all SPACs together is like judging the collective performance of every company in the S&P 500. With that said, the IPOX SPAC Index of 30 of the largest SPACs was down 2.08 percent year to date through June 30, 2021 after putting up strong numbers in previous years. Worse off is Morgan Creek's Exos SPAC Originated ETF, which launched on Jan. 26, 2021 and was down 16.1 percent through June 30, 2021.

Overall, I think it's wise to approach SPACs with skepticism. Because these entities are merely promising to invest in companies that meet their profile and criteria, investors don't know what they're ultimately getting in exchange for their investment dollars. Really, SPAC investors are buying into the reputations and past achievements of the SPAC's sponsors with the expectation that they can repeat their past successes. Because SPACs have recently raised so much capital that must be deployed within a two-year timeframe, there's also an increased risk of them investing in private companies that aren't the best targets. And even if all SPACs find great companies for acquisition, the tremendous capital available could result in SPACs competing over acquisition targets and paying prices that are too high under reasonable valuation assumptions. Furthermore, it's likely that regulators will continue to crack down on SPACs to protect ordinary investors' interests, which could ultimately make SPACs even less attractive investments than they've been in the recent past. For all these reasons, I advise investors and financial advisors to be very cautious when considering SPACs as part of an investment portfolio and long-term financial plan.

100% CPA MEMBERSHIP PROGRAM

To thank you for your support...

of the Illinois CPA Society and the profession, we are pleased to recognize these Illinois accounting firms with 100% of their CPA staff who are members.*

Adelfia LLC
Arnold, Behrens, Nesbit, Gray PC
Baker Tilly
Bansley & Kiener LLP
Bansley, Brescia & Co. PC
Barnes Givens & Barnes
BDO USA LLP
Benning Group LLC
Bernard A. Affetto & Co.
Borschnack, Pelletier & Co.
BrookWeiner LLC
Catalano, Caboor & Co.
CliftonLarsonAllen
Coleman & Associates
Cray, Kaiser Ltd.
Crowe LLP
Cygan Hayes Ltd.
Deborah K. Hannan CPA
Dennis Rose & Associates PC
Desmond & Ahern
Detterbeck Johnson & Monsen
Duffner & Company PC
Dunbar, Breitweiser & Company LLP
Eck, Schafer & Punke LLP
FSB&W
Gassensmith & Michalesko Ltd.
Gilbert Metzger & Madigan LLP
Gould & Pakter Associates LLC
Grant Thornton LLP
Gray Hunter Stenn LLP
GW & Associates PC
Hochfelder & Weber PC
Hoffman & Tranel PC
Holland & Company CPAs PC
Honkamp Krueger & Co. PC
Insight CPAs & Financial LLC
J.M. Abbott & Associates Ltd.
J.S. Richter Ltd.
John Kasperek Co. Inc.
John U. Smyth, CPA LLC
Jonker & Associates
Katz LLC
Kerber, Eck & Braeckel LLP
Kirkpatrick & Dahl PC
KPMG US LLP
Kutchins, Robbins & Diamond Ltd.
Larry J. Wolfe Ltd.
Lauterbach & Amen LLP
Leaf Dahl & Company Ltd.
Legacy Professionals LLP
Lerman, Sweeney & Company LLP
Lipschultz, Levin & Gray LLC
Lucas Group
Mack & Associates PC
Mann Weitz & Associates
Marcum LLP
McCullough Rossi & Co. Ltd.
McGreal & Company
MichaelSilver
O'Neill & Gaspardo LLC
Ostrow Reisin Berk & Abrams Ltd.
Pasquesi Sheppard LLC
PBG Financial Services Ltd.
PKF Mueller
PwC
Romolo & Associates LLC
Rub & Brillhart LLC
RubinBrown LLP
Sassetti LLC
Selden Fox Ltd.
SKDO CPAs & Advisors
The Charneske Group Ltd.
The Dolins Group Ltd.
Tighe, Kress & Orr PC
Topel Forman LLC
Trimarco Radencich LLC
West & Company LLC
Whitlock and Company PC
Wipfli LLP

ILLINOIS CPA SOCIETY
www.icpas.org

For more information on how your firm can be part of the 100% CPA Membership Program, please visit www.icpas.org.

*minimum of 2 CPAs