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The trouble with SPACS: Poor performance, investor complaints and SEC probes

Between the last quarter of 2020 and the first quarter of 2021, SPACs caused major waves, raising over $100B from investors. SPACs are non-operating, publicly listed companies whose sole purpose is to raise money on the public market and serve as a vessel to bring aboard companies, via reverse merger, who want IPO-money, without IPO-hassle or IPO-cost.

Now, just two years after their sudden surge in popularity, SPACs' sails appear to be in irons. Increasing scrutiny from regulators, complaints from investors, and overall poor performance are all signs that the SPAC ship may be sinking.

SPACs are often referred to as "blank check companies." The "blank" refers to the fact that SPAC investors generally don't know anything about the SPAC's potential targets. This uncertainty is a foundational and necessary feature of SPACs' abilities to keep their own IPO process simple and relatively cheap.

Due in part to this misalignment of interests between investors and SPAC parties, SPAC transactions are showing up on the SEC's radar at increasing rates. In July 2021, the SEC charged Stable Road Acquisition Company, SRC-NI and its CEO, Momentus, Inc. and its founder

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and former CEO with claims related to misleading investors. The SEC found that Momentus, Inc., the target — an early-stage space transportation company — represented to investors that it had commercially viable space transportation technology, when, in fact, its only missions failed to meet objectives.

Stable Road Acquisition and SRC-NI, the SPAC and the sponsor, respectively, repeated Momentus, Inc.'s claims, and claimed they had conducted exhaustive due diligence, when, in fact, they had not even reviewed the test results of Momentus, Inc.'s principal product. All parties, other than Momentus, Inc.'s CEO, settled, ultimately paying fines over $8M. The sponsor, SRC-NI, is also required to forfeit its compensation shares.

In addition to increased regulation, SPACs have also suffered from poor performance. For example, the resulting stock of one of the most touted SPAC deals, involving a merger between sports-betting company DraftKings with Diamond Eagle Acquisition Corp., and SBTech Global Limited, has experienced losses of over 50% between September 2021 and December 2021. Several other SPAC deals have fallen out altogether, with investors asking for their money back, and companies opting for the traditional IPO route.

With interest rate increases on the horizon, there is an increased probability that the SPAC ship will sink, or at least must dock its lines for the next decade or so.

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