

# THE SPAC REPORT

News, Information, and Analysis of Blank Check Companies

Volume II, No. 4

April 24, 2008

## D&O Insurance: Cheaper, Widely Available, but Not Yet Tested

by Joshua Sisco

Over the past year SPAC management and their legal advisors have been purchasing customized directors and officers (D&O) liability insurance that is tailored to the unique structure of the asset class. While there have been very few lawsuits of any type involving SPACs in the past, the market could become increasingly ripe for dispute as it matures.

“For years we have been worried about the sponsors’ indemnity,” said Doug Ellenoff, a partner at the New York law firm of **Ellenoff Grossman & Schole**.

SPACs have specific requirements when being insured against shareholder claims, he said. Often shareholders and target companies sign waivers up front promising not to go after the SPAC’s escrowed funds in a lawsuit, but protecting that cash is still necessary, he added.

So far, Ellenoff said, there have been no cases of what he calls “jilted lover’s syndrome,” where a target company feels the SPAC is at fault in a deal’s failure. However, there has been a significant increase in deals collapsing and the chances for claims from an unhappy target company are certainly heightened, he said.

Brendan Dolan, senior vice president at Marsh Inc.’s FINPRO Group, which serves as a D&O insurance broker on behalf of SPAC sponsors, said that the tailored approach to SPAC coverage is a recent occurrence, but one that must be taken seriously. “There are ‘exposures’ tied to a SPAC that would not be associated with the normal IPO D&O policy...including

policy length, trust indemnity obligations and change in control issues,” he said.

Ellenoff agreed with its importance, saying that it is relevant enough to have included a speaker, Dolan, on the SPAC panel that he moderated at **Roth Capital’s** Annual OC Growth Stock Conference in February.

But one prominent SPAC attorney believes there is very little risk for SPACs. There is always a trust waiver that says the target cannot go after the trust in court, and if shareholders don’t like a deal they get their money back, says David Miller, the managing partner at the New York law firm of **Graubard Miller**. Trust waivers accompany all merger documents, including non-binding letters of intent and definitive agreements, effectively eliminating trust account liabilities, says Miller.

Without operations to speak of, the management of a SPAC has little to indemnify itself against upfront. However, the standard structural characteristics, including time frame and acquisition threshold create a need for tailored coverage.

Like all IPOs, SPACs need protection against Sections 11 and 12 of the Securities Act of 1933, which cover materially false statements made in registration statements and prospectuses, according to Dolan. Unique needs for a SPAC include longer policy periods and extensions of coverage after a change in control of more than 50% takes place.


Traditional policies are written in 12-month intervals. If there is a

change in control of more than 50%, “coverage usually goes to runoff,” according to Jason Wallace at **Navigators Pro**, a primary D&O insurance carrier.

As an underwriter, the SPAC is rather transparent, according to Wallace, who said the firm has been writing policies for SPACs for approximately three years.

Wallace said any risk primarily lies within the management team itself. A number of items are reviewed, he said, including past M&A track record and any associated litigation, the sectors in which the SPAC is focusing its search, how much sector expertise of the management is used in the search, and any other past business associations and dealings.

Miller said coverage costs have come down significantly and the number of providers has increased to at least a dozen. At first, every \$1 million in coverage would cost \$50,000 to \$100,000. Now it can be purchased for less than \$20,000.

This insurance was not always easily obtainable, according to Miller. He said it took time and convincing before insurance companies were comfortable with covering SPACs. “We tried to get D&O [coverage] in the 1990s and no one would cover it. Around the end of 2004, there were a couple providers that decided to write coverage. We basically said, ‘It will be the extremely profitable, because there will be no claims.’” 

*Joshua Sisco can be reached at [josh@dealflowmedia.com](mailto:josh@dealflowmedia.com).*