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SEC's Proposed SPAC Rules:

A Closer Look at the Proposed Rules

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Introduction

On March 30, 2022, the commissioners of the Securities and Exchange Commission ("**SEC**") approved much-anticipated proposed rules relating to special purpose acquisition companies ("**SPACs**"). The proposed rules cover a wide range of topics, including expanding underwriter liability for disclosures in connection with de-SPAC transactions, target company and officer and director liability for such disclosures and expanding and revising disclosure requirements applicable to SPAC IPOs and de-SPAC transactions. While some of the proposed rules simply codify existing SEC staff positions and guidance or standard SPAC industry practice or are repetitive of existing rules, others are likely to have substantive impacts on SPACs, SPAC sponsors, SPAC IPO underwriters, private companies seeking to go public via de-SPAC transactions and other participants in de-SPAC transactions. Whether intentional or unintentional, likely consequences of the proposed rules, if adopted as is, are to defer access by some companies to capital markets for an extended period of time, reduce capital formation and innovation in the U.S. and deny ordinary investors access to investment opportunities not otherwise available to them.

The proposing release (the "**Proposing Release**") for the rules is available here.

The proposed rules were approved by a 3-1 vote of the SEC commissioners. Companies, investors and other interested parties that want to raise concerns, make suggestions, or provide information to support or flag issues with the proposed rules have until May 31, 2022 to provide written comments to the SEC. While the proposed rules may change in response to public comments or further consideration by the staff and commissioners of the SEC, and theoretically the SEC could determine not to adopt some or all of the rules, we expect many of the proposed rules to be adopted in largely their proposed form.

The proposed rules generally cover the following topics:

- Enhancing disclosure and investor protection;
- Revising the registration requirements for de-SPAC transactions;
- Projections disclosure; and
- Status of SPACs under the Investment Company Act of 1940.

We think it is helpful to distinguish among the following major categories of proposed rules:

- Substantive changes in the securities regulations;
- Technical changes, which should not substantively change the way SPACs, target companies and other SPAC market participants operate; and
- Conforming changes, where the SEC is codifying its existing positions or guidance or codifying what is existing practice by market participants, along with modest non-substantive changes.

We applaud the SEC's attempt to improve disclosure and the recognition that revisions are appropriate to reflect the fact that the substance of a de-SPAC transaction is often in essence an IPO by the target company. In addition, we welcome the elimination of uncertainty resulting from the SEC codifying its positions that were inconsistent with the previous rule and form requirements. However, we believe certain of the SEC's proposed rules and their underlying motivation suffer from, among other things, overstating regulatory arbitrage, failing to consider the structural and legal differences between de-SPAC transactions and IPOs, insufficiently aligning the treatment of companies that have gone public through de-SPAC transactions with those that went public via IPO and legislative encroachment. A proposal that the SEC describes as a mere "clarification" constitutes, in our view, a massive expansion of underwriter liability beyond that provided by Congress under the Securities Act of 1933 (the "**Securities Act**"). Moreover, the proposed rules deviate from the principles-based approach that the SEC has utilized for decades that results in efficient disclosure focusing on material items. Instead, the SEC is proposing to adopt a heavily prescriptive set of rules that will result in repetitive and immaterial disclosure in documents that are already too lengthy for many investors to digest.

The following is a discussion of the proposed rules, beginning with a discussion of the substantive changes in the securities regulations, along with those that have received the most attention from the market (even though some are largely technical and should not result in meaningful changes in practice), followed by a discussion of technical and conforming changes. Finally, we discuss other changes the SEC may consider, and the comment letter process, the need for comments in any challenge to new rules, and the process for adopting final rules.

Substantive and High Profile Changes

Underwriter Status and Liability in De-SPAC Transactions

A key concept in the Securities Act is the role, and liability, of "underwriters" in connection with registered offerings. The term underwriter is defined in Section 2(a)(11) of the Securities Act as "any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking." Underwriters, along with issuers, directors, officers, experts, etc., have liability for material misstatements and omissions in registration statements subject, in certain instances, to a due diligence defense.[1]

In the Proposing Release, the SEC alleges that every de-SPAC transaction constitutes a distribution of the combined company's securities, because the "result of a de-SPAC transaction, however structured, is consistent with that of a traditional initial public offering."[2]

Proposed Rule 140a would provide that underwriters of a SPAC's IPO who take steps to facilitate the de-SPAC transaction or any related financing transaction, or otherwise participate (directly or indirectly) in the de-SPAC transaction, will be deemed to be engaged in the distribution of the securities of the combined company resulting from the de-SPAC transaction. This would make those investment banks liable for any material misstatements or omissions appearing in the disclosure,[3] subject to a due diligence defense. The SEC purports to be merely interpreting the phrase "or participates or has a direct or indirect participation in [the distribution of any security],"[4] in addition to determining that all de-SPAC transactions are, in economic substance, a distribution of the target companies' securities to the SPACs' shareholders.

The Proposing Release states "receipt of compensation in connection with the de-SPAC transaction could constitute direct or indirect participation in the de-SPAC transaction."[5] The SEC argues that, because the SPAC IPO underwriters have deferred underwriting compensation that will only be received if a de-SPAC transaction is completed, the underwriter "has a strong financial interest in taking steps to ensure the consummation of the de-SPAC transaction."[6]

While not addressing underwriter liability of other participants in a de-SPAC transaction (*i.e.*, those that were not underwriters in the SPAC IPO) by rule, the SEC states that others, such as "financial advisors, PIPE investors, or other advisors, depending on the circumstances, may be deemed statutory underwriters . . . if they are purchasing from an issuer 'with a view to' distribution, are selling 'for an issuer,' and/or are 'participating' in a distribution."[7]

In our view, the SEC's position goes beyond a mere interpretation of the Securities Act and is substantively expanding the concept of an "underwriter" beyond that contemplated by Congress in adopting the Securities Act. While the Supreme Court has endorsed (in dicta) the concept of indirect participation in a distribution being sufficient to constitute an "underwriter,"[8] incidental participation is not sufficient. "[P]articipat[ion] only in non-distributional activities that may facilitate securities' offering by others . . ."[9] is not sufficient. Underwriter status is limited to those "people (or entities) responsible for distributing securities to the public, that is, on those engaged in the public offering."[10]

The securities laws do not mandate that every distribution have an underwriter, but impose liability on those that act in the capacity of an underwriter. The SEC seems inclined to attempt to mandate that there be an underwriter for de-SPAC transactions in order to "screen the multitude of issuers seeking access to the capital markets,"[11] but many of the cases cited by the SEC in explaining the importance of the underwriter role and liability support the conclusion that the investment banks participating in de-SPAC transactions are not in fact underwriters. The SEC quotes *SEC v. Richmond* for the proposition that "[i]nvestors . . . rely on [an implicit representation from an underwriter that it has done diligence] which has a direct bearing on their appraisal of the reliability of the representations in the prospectus."[12] In a footnote in the Proposing Release, the SEC quotes *Sanders v. John Nuveen & Co., Inc.*, 524 F.2d 164, 1069-70 (7th Cir. 1975), for the proposition that, among other things, "the relationship between the underwriter and its customers implicitly involves a favorable recommendation of the issued security."[13] However, in de-SPAC transactions, even assuming they involve a distribution, the investment banks do not have such customers. Their names do not appear on the cover of the prospectus, and the investing public is not relying on the role of the investment banks to make an investment decision. Financial motivations notwithstanding, the SPAC IPO underwriters may have no actual participation in the de-SPAC transaction, and even when they do they are not responsible for the public disclosure. To the extent they are named in the disclosure, it is merely to describe their roles, which do not relate to the de-SPAC's alleged distribution of securities under proposed Rule 145a. As proposed by the SEC, remote "participation" in the de-SPAC transaction by an investment bank or other advisors — for example, acting as lead arranger for a credit facility for the resulting company — would transform such investment bank or other advisors from incidental participants into underwriters for purposes of the Securities Act. This goes well beyond the definition of "underwriter," beyond the congressional intent from 1933, and is inconsistent with case law interpreting both.

To the extent the SEC or Congress determines that an underwriter should be mandated for every de-SPAC transaction, that would be more appropriately handled via legislation or the SEC could mandate a new role for an investment bank in de-SPAC transactions for all exchange-listed SPACs.[14] As drafted, the proposed rule is unduly vague, and we believe specificity as to which investment banks and advisors may be exposed to potential underwriter liability is imperative.

In terms of impact on SPACs, SPAC IPOs and de-SPAC transactions, while the proposed rules are pending and assuming they are adopted as proposed, institutions involved in SPAC IPOs and de-SPAC transactions will likely attempt to establish a due diligence defense against potential liability, or seek ways to distance themselves from the de-SPAC transaction sufficiently as to not constitute statutory underwriters (although this may be difficult, given the breadth and vagueness of the SEC's new interpretation). This has the likelihood to delay de-SPAC transactions and increase costs for de-SPAC transactions, and will likely result in incremental negotiated contractual rights for the SPAC IPO underwriters and investment banks participating in a de-SPAC transaction. Some institutions may refrain from participating in de-SPAC transactions altogether, even where they did not serve as IPO underwriters, due to the breadth of the SEC's "interpretation" of Section 2(a)(11). Taken together, this will increase uncertainty for SPAC market participants across the spectrum. For future SPAC IPOs and de-SPAC engagements, investment banks will likely seek strong contractual rights to participate in diligence, comment on the disclosure documents, and potentially withdraw at their option.

Elimination of PSLRA Safe Harbor

The SEC is proposing to amend the definition of "blank check company" for purposes of the Private Securities Litigation Reform Act of 1995 (the "**PSLRA**") to mean "a company that has no specific business plan or purpose or has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies, or other entity or person." This would make SPACs ineligible for the safe harbor provided by the PSLRA.

The PSLRA provides a safe harbor from liability for forward-looking statements when, among other things, a forward-looking statement is identified as such and is accompanied by meaningful cautionary statements. The safe harbor currently does not apply to statements made in IPOs, to statements made by certain types of registrants, such as limited partnerships or blank check companies, or to statements made in connection with certain types of transactions, such as tender offers. The safe harbor does not protect against false or misleading statements made with actual knowledge that the statement was false or misleading. SPACs that raise more than $5 million in their IPO are excluded from the current definition of blank check company referenced in the PSLRA, and thus the PSLRA safe harbor is generally considered to be available for forward-looking statements made in connection with de-SPAC transactions.[15] However, the SEC's proposed change to the definition of blank check company referenced in the PSLRA would exclude forward-looking statements made in connection with de-SPAC transactions.

Even if the proposed amendment is adopted, parties to a de-SPAC transaction may still be able to rely on the "bespeaks caution" doctrine for any forward-looking statements included in the disclosure. This doctrine was developed prior to the introduction of the PSLRA safe harbor and provides that a forward-looking statement "accompanied by sufficient cautionary language is not actionable because no reasonable investor could have found the statement materially misleading."[16] The PSLRA was based on aspects of this doctrine but it did not replace the doctrine, which is especially valuable for parties that are excluded from the PSLRA safe harbor. Parties should still take care to ensure that there is a reasonable basis for the forward-looking statements and that there are no undisclosed facts that may undermine the accuracy of such statements.

The SEC explains that this change is necessary in order to treat forward-looking statements made in connection with de-SPAC transactions the same as forward-looking statements made in traditional IPOs and thus ensure that the parties exercise the same level of care in preparing forward-looking statements, such as projections. However, one key difference between IPOs and de-SPAC transactions that the SEC does not address is that a SPAC in a de-SPAC transaction is typically required to disclose the target company's projections if the SPAC's board relied on such projections when approving the de-SPAC transaction.

Projections will likely continue to be used in de-SPAC transactions, because the SPAC board will need them for valuation purposes (which is why you see projections used in fairness opinions, public company mergers, etc.), but there will be added scrutiny of projections, particularly by the investment banks that may be "underwriters." There may also be an inclination to reduce or limit the use of projections in PIPE marketing presentations or investor presentations.

Notwithstanding the vast number of times repeated to the contrary, projections are permitted in registration statements for IPOs. In fact, there are certain industries and structures where projections are effectively required and fully accepted by investors, underwriters and the SEC.[17] Real estate investment trusts, YieldCos and master limited partnerships often include a forecast in their IPO registration statements to demonstrate their ability to pay dividends.

Enhanced Projections Disclosure

In response to perceived issues with the use of projections in SEC filings made by SPACs, the SEC is proposing to amend Item 10(b) of Regulation S-K and create new Item 1609 of Regulation S-K. The amendments to Item 10(b) are intended to expand and update the SEC's views and guidance for registrants on the use and presentation of projections in SEC filings, and new Item 1609 will mandate specific disclosures relating to financial projections presented in de-SPAC transactions.

Proposed Amendments to Item 10(b) of Regulation S-K

The SEC is proposing to amend Item 10(b) to present the SEC's updated views on the use of projected financial information. The proposed amendments would continue to state the SEC's view that projected financial information included in SEC filings must have a reasonable basis, and would further state that:

- Any projected financial measures that are not based on historical financial results or operational history should be clearly distinguished from projected measures that are based on such historical financial results or operational history;
- It generally would be misleading to present projections that are based on historical financial results or operational history without presenting such historical measure or operational history with equal or greater prominence; and
- The presentation of projections that include a non-GAAP financial measure should include a clear definition or explanation of the measure, a description of the GAAP financial measure to which it is most closely related, and an explanation of why the non-GAAP financial measure was used instead of a GAAP measure.

Since current Item 10(b) refers to projections regarding the future performance of a "registrant," it may be unclear whether Item 10(b) currently applies to projections of a target company where the target company is not the "registrant" for that filing. Accordingly, the SEC is also proposing to amend Item 10(b) to clarify that the guidance therein also applies to any projections of future economic performance of any person other than the registrant, such as the target company in a de-SPAC transaction, that are included in the registrant's SEC filings.

Proposed Item 1609 of Regulation S-K

The SEC is proposing to add a new Item 1609 to Regulation S-K, which would only apply to SEC filings made in connection with de-SPAC transactions and proposes to mandate specific disclosures that would be required in such filings. These additional disclosure requirements are intended to assist investors in assessing the basis for any projections included in filings made in connection with a de-SPAC transaction and determining the extent to which they should rely on such projections.

Proposed Item 1609 would require disclosure of:

- The purpose for which any projections disclosed by the registrant were prepared and the party that prepared them;
- All material bases of the disclosed projections and all material assumptions underlying the projections, as well as any factors that may materially impact such assumptions, including discussion of:
    - any factors that may cause the assumptions to no longer be reasonable;
    - material growth rates or discount multiples used in preparing the projections; and
    - the reasons for selecting such growth rates or discount multiples;
- Whether the disclosed projections still reflect the view of the board of directors or management of the SPAC or the target company, as applicable, as of the date of the SEC filing in which such projections are included.
    - If the disclosed projections do not reflect the view of the board of directors or management of the SPAC or the target company, as applicable, as of the date of the relevant SEC filing, then a discussion of the purpose of disclosing the projections and the reasons for any continued reliance by the board of directors or management would also be required.

In terms of impact, these proposed rules are likely not as significant as some of the others. Much of the disclosure that would be required under the proposed amendments to Item 10(b) and new Item 1609 is already being made based on industry practice or in response to recent SEC comments, such that the proposed rules should not substantively change the way SPACs use projections. The rules may result in more standardized disclosure and would call for a new explicit statement that projections do or do not continue to reflect the view of the SPAC board.

Fairness Disclosure

Of the proposed rules, proposed Item 1606 of Regulation S-K is one that has received particular attention. Modeled after Item 1014(a) of Regulation M-A, which sets forth disclosure requirements for going private transactions, proposed Item 1606(a) would require disclosure as to whether the SPAC reasonably believes that "the de-SPAC transaction and any related financing are fair or unfair to unaffiliated security holders of the [SPAC]."[18] While inclusion of such a statement would be a new requirement and may seem concerning on its face to some, in light of the fiduciary duties applicable to SPACs and their directors and officers, making a statement regarding fairness itself is not likely to be significant as a practical matter. Moreover, the required incremental disclosures regarding the determination (specifically the bases for the determination and factors considered in determining fairness) would likely be redundant with the standard disclosure of the SPAC board's reasons for approval of the de-SPAC transaction.

The new requirements would not mandate that the SPAC board receive a fairness opinion or third party valuation. Nevertheless, SPAC boards may be more likely to seek fairness opinions or third party valuations, which may be what the SEC is hoping to achieve. In the Proposing Release, the SEC comments on the purported benefits of fairness opinions obtained in M&A transactions and estimates the costs of obtaining a fairness opinion in a de-SPAC transaction "to the extent that the proposed required disclosures with respect to the fairness or unfairness of the proposed business combination would increase the use of fairness opinions."[19] Despite the SEC's stated position that the proposed rules are intended to better align the disclosures made in de-SPAC transactions with those given in traditional IPOs, there a number of instances where these proposed rules go well beyond what is required in traditional IPOs, and proposed Item 1606(a) is one such example.

Proposed Items 1606(b)-(e) largely track Item 1014 of Regulation M-A verbatim but for SPAC-terminology changes, and would require the following:

- Disclosure of any director who voted against or abstained from voting on approval of the de-SPAC transaction and any related financing;
- Discussion in reasonable detail of the material factors considered in determining fairness of the de-SPAC transaction, including, if practicable, the weight of each such factor considered. Such factors are to include "the valuation of the target company, the consideration of any financial projections, any report, opinion or appraisal described in [proposed Item 1607] and the dilutive effects described in [proposed Item 1604(c)]";
- Disclosure if approval of a majority of the unaffiliated security holders is required;
- Disclosure if a majority of the non-employee directors of the SPAC has retained an unaffiliated representative "to act solely on behalf of the unaffiliated security holders" for purposes of negotiating the terms of the transaction and/or preparing "a report concerning the fairness of the de-SPAC transaction or any related financing transaction"; and
- Disclosure if the transaction was approved by a majority of the directors of the SPAC who are not employees of the SPAC.

We believe the disclosure required by proposed Items 1606(b)-(e) is generally already required in registration statements and/or proxy statements and is accepted disclosure practice, so codifying these requirements in the context of SPAC-specific disclosures is unnecessary.

Reports, Opinions, and Appraisals

Proposed Item 1607 would require filing a copy of, as well as disclosure of a number of specific items relating to, “any report, opinion or appraisal [received] from an outside party relating to the consideration or the fairness of the consideration to be offered to security holders or the fairness of the de-SPAC transaction or any related financing transaction to the [SPAC], SPAC sponsor or security holders who are not affiliates.”[20] For the most part, proposed Item 1607 tracks Item 1015 of Regulation M-A, which dictates certain disclosure required in filings involving going private transactions. Registration statements and proxy statements currently require disclosure of information required by Rule 1015(b).[21]

Proposed Item 1607(b) would require disclosure of the following:

- the identity and qualification of the provider of the report, opinion or appraisal;
- the method of selecting the provider;
- any material relationship existing in the last two years or that is being contemplated and any related compensation that was or is to be received between the provider and its affiliates and the SPAC, SPAC sponsor and their affiliates; and
- whether the provider or the SPAC or SPAC sponsor recommended the amount of consideration to be paid to the target company and its security holders or the valuation of the target company.[22]

The required disclosure set forth in proposed Item 1607(b) also would apply to any negotiation or report concerning the transaction provided by an unaffiliated representative retained to act solely on behalf of unaffiliated security holders of the SPAC as described in proposed Item 1606(d).

Proposed Item 1607(b)(6) would require a summary of the negotiation, report, opinion or appraisal, including the procedures followed; the findings and recommendations, the bases for and methods of arriving at such findings and recommendations; instructions received from the SPAC or SPAC sponsor; and any limitation imposed by the SPAC or SPAC sponsor on the scope of the investigation.

Finally, proposed Item 1607(c) would require that all reports, opinions and appraisals required by Item 1607(a) be filed as exhibits to the registration statement or included in the proxy statement. Forms S-4 and F-4 currently expressly require that reports, opinions or appraisals described in the prospectus be filed as exhibits to the registration statement. Including such reports, opinions or appraisals in a proxy statement would go beyond the current requirements for proxy statements, but proposed Rule 145a would effectively eliminate proxy statement-only de-SPAC transactions. Similar to the required statement regarding fairness of the transaction, this requirement goes beyond required disclosure in IPO registration statements.

Investment Company Act Safe Harbor

Recent civil lawsuits and academic articles have suggested that SPACs are unregistered investment companies by virtue of investing in short-term U.S. government securities while they hunt for a target company. In the Proposing Release the SEC states that “certain SPAC structures and practices may raise serious questions as to their status as investment companies,”[23] and provides as examples “invest[ing] in securities not permitted by the proposed safe harbor, actively manag[ing] [the SPAC's] portfolio or hold[ing] itself out in a manner that suggests investors should invest to gain exposure to the portfolio it holds prior to the de-SPAC transaction." The SEC states that a SPAC raises similar concerns if it invests in securities (including short-term U.S. government securities) for a lengthier period of time without identifying a target company and that it is more likely a SPAC will appear to be an investment company if it seeks to acquire a minority interest in a target company with the intention of being a passive investor (perhaps a reference to the abandoned de-SPAC transaction by Pershing Square Tontine Holdings).

The SEC is proposing a new Rule 3a-10 under the Investment Company Act of 1940 that would establish a safe harbor from investment company act status for SPACs so long as certain conditions are met.

The conditions of the proposed safe harbor would be:

"(a). . . (1) The SPAC's assets consist solely of Government securities, securities issued by government money market funds as defined in [Investment Company Act Rule] 2a-7(a)(14),[[24]] and cash items prior to completion of the de-SPAC transaction;

(2) The assets set forth in paragraph (a)(1) of this section are not at any time acquired or disposed of for the primary purpose of recognizing gains or decreasing losses resulting from market value changes;

(3) The SPAC:

(i) Seeks to complete a single de-SPAC transaction as a result of which:

(A) The surviving company, either directly or through a primarily controlled company, will be primarily engaged in the business of the target company or companies, which business is not that of an investment company, and

(B) The surviving company will have at least one class of securities listed for trading on a national securities exchange;

(ii) Files a Form 8-K with the Commission, no later than 18 months after the effective date of its initial registration statement, disclosing an agreement to engage in the de-SPAC transaction with at least one target company; and

(iii) Completes the de-SPAC transaction no later than 24 months after the effective date of its initial registration statement.

(4) Any assets of the SPAC:

(i) That are not used in connection with the de-SPAC transaction; or

(ii) In the event of a failure of the SPAC to file a Form 8-K within the time frame set forth in paragraph (a)(3)(ii) of this section or complete a de-SPAC transaction within the time frame set forth in paragraph (a)(3)(iii) of this section

will be distributed in cash to investors as soon as reasonably practicable thereafter;

(5) The SPAC is primarily engaged in the business of seeking to complete a single de-SPAC transaction, as set forth in paragraphs (a)(3) of this section and evidenced by:

(i) The activities of its officers, directors and employees;

(ii) Its public representations of policies;

(iii) Its historical development; and

(iv) An appropriate resolution of its board of directors, which resolution or action has been recorded contemporaneously in its minute books or comparable documents; and

(6) The SPAC does not hold itself out as being primarily engaged in the business of investing, reinvesting or trading in securities."[25]

Condition (1), that the "SPAC's assets consist solely of Government securities . . .," substantively codifies the existing behavior by SPACs. Current SPAC practice is to limit investment of the assets in the trust account to U.S. government securities within the meaning of Section 2(a)(16) of the Investment Company Act having a maturity of 185 days or less, or in money market funds meeting the conditions of paragraphs (d)(1), (d)(2), (d)(3), and (d)(4) of Rule 2a-7 promulgated under the Investment Company Act, which invest only in direct U.S. government treasury obligations. In lieu of an investment of the assets in the trust account, they can be held in cash. However, the proposed condition is slightly more lenient than current SPAC practice, in that the safe harbor would not include a maturity limit for Government securities,[26] and the proposed condition would not include the "Risk-limiting conditions" set forth in Rule 2a-7(d).[27]

Condition (2), that the assets of the SPAC are not "at any time acquired or disposed of for the primary purpose of recognizing gains or decreasing losses resulting from market value changes" has been described by the SEC as a condition that the SPAC not "actively manage its portfolio." This is consistent with how SPAC management teams already operate.

Condition (3) would require that the SPAC seek to undertake "a single de-SPAC transaction" as a result of which the surviving company, roughly speaking, is listed on a national securities exchange and is not an investment company. Most importantly, this condition would require the de-SPAC transaction to be announced within 18 months of the SPAC's IPO[28] and closed within 24 months after the SPAC's IPO. These time limits are unduly restrictive, and by the SEC's own estimation would not have been met by approximately 43% of SPACs that completed de-SPAC transactions between 2016 and 2019.[29] Moreover, the surveys cited by the SEC are dated, and more recent transactions have been taking longer (in part because the SEC review and comment periods have been more protracted). Since the beginning of 2022, the average duration from announcement to closing of completed de-SPAC transactions has been almost seven months as compared to approximately five months in the survey of 2016 to 2019 transactions cited by the SEC.

In our view, the proposed deadlines for signing and closing do not match the purported risk that investors might view long-in-the-tooth SPACs more like investment companies — if investors were investing in SPACs to gain exposure to short-term U.S. government securities, investing in a recently minted SPAC (with more time to maturity) would be a better strategy, as there would be a longer period to benefit from the investments. In practice, investors seeking such exposure would invest in actual mutual funds invested in such securities, as there is no guarantee that SPACs will invest the funds in the trust account. Importantly, SPAC management has little ability to profit from investments in securities made with the funds held in the trust account. The concept that a SPAC management team would engage in "regulatory arbitrage . . . to operate like an investment company without investment company registration"[30] is nonsensical, as the redemption requirement means that management has zero incentive to manage the trust account assets other than to preserve capital. So long as the directors and officers of the SPAC are focusing on acquiring operating companies or assets, we believe arbitrary deadlines should be avoided, which would allow SPACs to be treated similarly to other companies with substantial cash to be invested for capital preservation purposes.[31]

The requirement that the SPAC seek a transaction in which the resulting company will be listed on a national securities exchange bears no relationship to whether the SPAC is an investment company, and should be eliminated. While exchange listing is the goal for almost every de-SPAC transaction, it is possible that the company may not be eligible due to, among other things, excessive redemptions and we view there to be no correlation between whether the surviving company is listed on an exchange and investors viewing the SPAC as an investment company.

The requirement that the SPAC undertake "a single de-SPAC transaction" would not prevent a multi-target de-SPAC transaction, and seems to miss the point that once a de-SPAC transaction is completed, the surviving company is no longer a SPAC. However, it could be read to prevent the target company from signing further business acquisitions during the pendency of the de-SPAC transaction, which would adversely affect companies going public in this manner as compared to an IPO.

Condition (4) would require the SPAC to distribute all assets not used in the de-SPAC transaction to investors promptly thereafter. This condition is described by the SEC as ". . . the SPAC would be unable to seek another de-SPAC transaction with its remaining assets, or otherwise continue to operate as a SPAC. . .," and as a supplement to the condition that the SPAC undertake only a single de-SPAC transaction.[32] This condition ignores the practical reality that most de-SPAC transactions are financing transactions for the target company — just like in an IPO, the resulting public company typically retains substantial cash on its balance sheet in order to fund its future operations. We believe this condition should be eliminated, because after completion of the de-SPAC transaction the public company is no longer a SPAC, and any acquisitions it subsequently makes are no longer de-SPAC transactions.

Condition (4) would also require all assets (not just the trust account assets) to be distributed if the SPAC fails to announce a de-SPAC transaction within 18 months or consummate a de-SPAC transaction within 24 months. Whether a SPAC could rely on the safe harbor for its first 18 or 24 months of operation, and then rely on a different exemption or exclusion thereafter (*i.e.* without distribution of all assets and liquidation) is unclear. The SEC states in the Proposing Release that the SPAC could not rely on the "transitory" exemption under Rule 3a-2 after relying on the proposed Rule 3a-10 safe harbor (or vice versa), but does not expressly preclude an alternative exclusion (such as liquidating the investments in the trust account and exclusively holding cash).

Conditions (5) and (6) would require the SPAC to be primarily engaged in hunting for a de-SPAC transaction, and not hold itself out as being primarily engaged in the business of investing, reinvesting or trading in securities. This effectively states what SPACs are in substance doing (as, for example, the directors and officers of the SPAC spend little to no time dealing with the investment of the trust assets in securities, but instead focus on identifying, negotiating, and consummating a de-SPAC transaction).

In our view the vast majority of SPACs do not constitute investment companies under applicable law,[33] do not undertake the practices that the SEC cites as raising questions as to whether they are investment companies (other than perhaps taking a long time to identify a target company and consummate a transaction), and do not present the risks of investor harm that the Investment Company Act was adopted to protect against. SPACs' assets are invested in low risk, high quality U.S. government debt securities as a capital preservation mechanism, and not for speculative purposes. Moreover, because of the trust account structure and redemption rights, SPAC officers and directors have no motivation to manage the investments for their own interests. While a safe harbor would be welcome, one that leaves almost half of the companies that might seek to rely on it sailing the open seas, without real justification based on the investor harms the Investment Company Act was adopted to protect against, is inappropriate.

In addition, the impact of the proposed safe harbor on existing SPACs could be meaningful. For SPACs that are approaching, or have already exceeded, the deadlines in the proposed safe harbor, the SEC's statements in the Proposing Release introduce substantial uncertainty, as the SEC is effectively suggesting that there is a strong risk that the SEC will view them as unregistered investment companies. This may make target companies, investment banks and others less willing to transact, or require such SPACs to hold cash in lieu of investing in U.S. government securities (potentially decreasing the return on the cash and potentially substantially increasing risk to the public investors).

Technical and Conforming Changes

De-SPACs Deemed a Sale to SPAC Shareholders

New Rule 145a would deem that a de-SPAC transaction constitutes a sale of securities to the SPAC's shareholders for purposes of the Securities Act. This would require the filing of a Form S-4 or Form F-4 for most de-SPAC transactions. Under current rules, depending on the structure of the de-SPAC transaction and other considerations, a de-SPAC transaction can be accomplished using only a proxy statement.

While introducing certain technical differences in applicable liability regimes, this will likely not change the behavior of companies engaging in de-SPAC transactions. First, the burden for plaintiffs to plead securities claims based on a registration statement is not dramatically different than for a proxy statement. While claims under Section 11 of the Securities Act alleging misleading statements in a registration statement are somewhat easier to plead because they require no allegation of the defendants' mental state (and are subject only to a due diligence defense for non-issuers), claims alleging misleading statements in a proxy statement under Section 14(a) of the Securities Exchange Act of 1934 (the "**Exchange Act**") need only plead the defendants acted negligently.[34] Section 14(a)'s negligence standard, although a somewhat higher threshold than Section 11's effectively strict liability standard, does not present plaintiffs with anywhere near the barrier of the requirement to plead an intent to defraud under some other securities law provisions (for example, Rule 10b-5). Moreover, structuring considerations other than securities laws often require that the target company or one of its newly formed subsidiaries serve as the resulting company, which requires a registration statement for the offering of securities to the SPAC's existing public stockholders. While the SEC suggests that the change is to prevent private companies from using a shell company "to avoid the disclosure, liability and other provisions applicable to traditional registered offerings,"[35] in practice, exchange-listed SPACs provide substantially the same disclosure regardless of whether the transaction involves a registration statement or only a proxy statement. Moreover, the SPAC has similar obligations for any misstatements or omissions made in a proxy statement as in a registration statement.

Private Operating Company as Co-Registrant to Form S-4 and Form F-4

The SEC is proposing to amend Form S-4 and Form F-4 to require that the SPAC and the target company be treated as co-registrants. Specifically, the SEC is proposing to amend the signature instructions to Forms S-4 and F-4 to state that, if a SPAC is offering its securities in a de-SPAC transaction that is registered on the form, the term "registrant" for purposes of the signature requirements of the form would mean the SPAC and the target company. Depending on the structure of the de-SPAC transaction, historically only the SPAC or a newly formed subsidiary of the SPAC or the target company has been the registrant in most de-SPAC transactions[36] and therefore subject to liability under Section 11 of the Securities Act, which prohibits issuers, officers, underwriters and others from making material misstatements or omissions in registration statements. The SEC's proposal would make the additional signatories to the form, including the principal executive officer, principal financial officer, controller/principal accounting officer, and a majority of the board of directors or persons performing similar functions of the target company, liable (subject to a due diligence defense for all parties other than the SPAC and the target company) under the Securities Act for any material misstatements or omissions made in the Form S-4 or Form F-4.

This proposal would not radically transform the securities law landscape for target companies and their directors and officers. As a practical matter, target companies already face *de facto* exposure arising from SPAC registration statements, because any liability for a misstatement typically arises post-closing after the two businesses have combined. Moreover, both parties and their directors and officers are already potentially subject to liability under the Exchange Act with respect to statements made relating to the de-SPAC transaction due to their participation in the solicitation of proxies in connection with the SPAC's shareholder meeting. And, as the SEC notes, the target company and its affiliates may already be subject to enforcement actions by the SEC under Section 17(a) of the Securities Act (prohibiting any person from obtaining money or property in a manner that would operate as a fraud or deceit upon the purchaser, but which is generally held not to create a private right of action) and Section 10(b) of the Exchange Act and Rule 10b-5 under the Exchange Act (prohibiting fraud in connection with the purchase and sale of any security), as well as private rights of action under Rule 10b-5 under the Exchange Act.

However, the SEC's proposal would meaningfully expand potential liability for target company directors and officers in at least two respects. First, requiring them to sign the SPAC's registration statement will mean they can be deemed to have "made" the statements therein, which will considerably expand the number of statements potentially serving as a basis for liability.[37] Second, even apart from increasing the number of potential misstatements for which target company officers and directors may be liable, claims brought under Section 11 for misstatements in a registration statement are considerably easier for a plaintiff to plead than the claims under Rule 10b-5 for other misstatements that target company officers and directors currently face. Rule 10b-5 claims require a specific pleading that the defendant acted with scienter, meaning an intent to defraud.[38] By contrast, Section 11 claims do not require any pleading of the defendant's mental state.[39] The SEC's proposal seems unlikely to materially increase the number of SPAC lawsuits alleging misstatements, the statutes or rules sued under, or the damages claimed, but would likely lead to the naming of additional defendants in those lawsuits.

New Subpart 1600 of Regulation S-K

As part of the new rules, the SEC is proposing to add a new Subpart 1600 of Regulation S-K specifically applicable to SPACs. Regulation S-K provides non-financial disclosure requirements that are cross referenced from applicable SEC forms, such as Form S-1, Form S-4, Form F-4 and Schedule 14A. Subpart 1600 would set forth specialized disclosure requirements regarding the SPAC sponsor, conflicts of interest and dilution.

Definitions

The SEC is proposing to adopt the following new definitions:

"(a) *de-SPAC transaction*. The term *de-SPAC transaction* means a business combination such as a merger, consolidation, exchange of securities, acquisition of assets, or similar transaction involving a special purpose acquisition company and one or more target companies (contemporaneously, in the case of more than one target company).

(b) *Special purpose acquisition company (SPAC)*. The term *special purpose acquisition company* means a company that has indicated that its business plan is to:

(1) Register a primary offering of securities that is not subject to the requirements of § 230.419 (Rule 419 under the Securities Act);

(2) Complete a de-SPAC transaction within a specified time frame; and

(3) Return all remaining proceeds from the registered offering and any concurrent offerings to its shareholders if the company does not complete a de-SPAC transaction within the specified time frame.

(c) *SPAC sponsor*. The term *SPAC sponsor* means the entity and/or person(s) primarily responsible for organizing, directing or managing the business and affairs of a special purpose acquisition company, other than in their capacities as directors or officers of the special purpose acquisition company as applicable.

(d) *Target company*. The term *target company* means an operating company, business or assets."[40]

We note that the proposed definition of "special purpose acquisition company" is not limited to companies listed on a national securities exchange. It would include shell companies traded in over-the-counter markets, which are not what we would generally consider to be "SPACs." Exchange listing rules applicable to listed SPACs require, among other things, a proxy statement in most de-SPAC transactions, while OTC-listed SPACs may be able to announce and consummate a de-SPAC transaction without a SPAC shareholder vote. We think a logical distinction could be drawn based on exchange listing, rather than on whether the offering is by a blank check company and therefore subject to Rule 419. More importantly, the proposed definition is unclear as to whether a SPAC ceases to be a SPAC for purposes of these rules after consummation of a de-SPAC transaction, which could result in uncertainty as to the application of some of the proposed rules post de-SPAC transaction, and potential disparity between companies that go public via de-SPAC transactions as opposed to traditional IPOs.[41]

The proposed definition of "SPAC sponsor" is vague. For many SPACs, the persons primarily responsible for organizing,[42] directing and managing the business and affairs of the SPAC are the SPAC's directors and officers, who are expressly excluded from the definition. We believe that a definition for SPAC sponsor is unnecessary, and the purpose of the term (largely tied to conflicts of interest, experience, related party transactions and compensation disclosure) could be satisfied by directly referring to the directors, officers and affiliates of the SPAC, along with their respective affiliates, in the rules.

The definition of “target company” includes assets. While it is possible, albeit rare, for a SPAC to consummate a de-SPAC transaction in which it only acquires assets, the use of “target company” in some of the other proposed rules produces anomalous results (such as the concept that assets may be a co-registrant on a registration statement).

Disclosure Regarding SPAC Sponsors

Proposed Item 1603(a) would require enhanced disclosure about the SPAC sponsor, its affiliates and any other promoters of the SPAC in connection with SPAC IPOs and de-SPAC transactions, including:

- The experience, material roles and responsibilities of each of the parties listed above;
- Any agreement or arrangement with respect to (1) the determination of whether to proceed with a de-SPAC transaction or (2) the redemption of securities;
- The controlling persons of the SPAC sponsor and any person with a direct or indirect material interest in the SPAC sponsor;
- An organizational chart reflecting the relationship between the SPAC sponsor, the SPAC and its affiliates;
- Tabular disclosure of the material terms of any lock-up agreements; and
- The compensation of the SPAC sponsor, its affiliates or other promoters.

Much of the additional disclosure that would be required under proposed Item 1603(a) merely codifies existing disclosure practices of the last several years, including disclosure added in response to recent SEC comments.

Moreover, the Proposing Release appears to blur the lines between the roles and responsibilities of the SPAC sponsor and that of the SPAC board. If the SPAC sponsor is actually managing and directing the SPAC like the SEC suggests, then the SPAC sponsor’s directors and officers would constitute the directors and officers of the SPAC for purposes of both the Securities Act and the Exchange Act. As a result, many of the proposed disclosure items would already be covered under existing disclosure requirements that require such disclosure vis-à-vis the directors and officers of the SPAC and their affiliates. We recommend revising the disclosure items of proposed Item 1603(a) to focus solely on the directors, officers and affiliates of the SPAC. Similarly, the additional compensation disclosure should be revised to refer instead to all equity and rights to cash held by the SPAC directors and officers and their affiliates.

Conflicts of Interest Disclosure

The SEC is proposing in Item 1603(b) to require disclosure of any actual or potential material conflict of interest between (1) the SPAC sponsor or its affiliates or the SPAC’s officers, directors or promoters, and (2) unaffiliated security holders. The SEC notes that this would include any conflict of interest in determining whether to proceed with a de-SPAC transaction and any conflict of interest arising from the manner in which a

SPAC compensates the SPAC sponsor or the SPAC's officers and directors, or the manner in which the SPAC sponsor compensates its own officers and directors. The SEC is also proposing to require disclosure regarding the fiduciary duties that each officer and director of a SPAC owes to other companies.

This required disclosure would largely codify existing disclosure practice. In SPAC IPOs, SPACs routinely disclose conflicts of interest in the Summary, Risk Factors and Management sections of Form S-1 related to, among other things, the following: (1) potential competition (both with respect to investment opportunities and time within which to complete a de-SPAC transaction) with SPACs and other investment vehicles affiliated with the SPAC sponsor or the SPAC's directors and officers, (2) potential post-closing roles that the SPAC's directors and officers may be offered by the target company, (3) potential affiliations between the SPAC and the target company and (4) the SPAC sponsor's and the SPAC's directors' and officers' investment in the SPAC's securities. SPACs also routinely include disclosure regarding the specific fiduciary duties owed by the SPAC's directors and officers. In de-SPAC transactions, SPACs also disclose conflicts of interests in response to the existing requirements of Item 5 of Schedule 14A, which are also incorporated into the requirements of Form S-4 and Form F-4.

Dilution Disclosure

Proposed Regulation S-K items[43] would require disclosure regarding potential dilution in registration statements and proxy statements for SPAC IPOs and de-SPAC transactions. Material potential sources of future dilution would be required to be disclosed, including tabular disclosure about potential dilution that may be borne by non-redeeming shareholders, along with a sensitivity analysis showing potential dilution under a range of redemption levels. The SEC notes the following as potential sources of dilution: SPAC sponsor economics, underwriting fees, warrants and convertible securities, and financing transactions.

Much of this disclosure has already been included in registration statements and proxy statements filed in connection with de-SPAC transactions in response to recent SEC comments.

Prospectus Cover Page and Prospectus Summary Disclosure

Proposed Item 1602 would require certain disclosures be highlighted on the prospectus cover page and in the prospectus summary in plain English.

For SPAC IPOs, proposed Item 1602(a) would require disclosure of the following on the prospectus cover page:

- Time period required to consummate a de-SPAC transaction and whether the time period may be extended;
- Redemptions;
- Compensation received, or that may be received, by the SPAC sponsor and its affiliates;
- Dilution, including simplified tabular disclosure; and
- Conflicts of interest.

For de-SPAC transactions, proposed Item 1604(a) would require inclusion of the following on "the outside front cover of the prospectus":

- Information regarding the fairness of the de-SPAC transaction;
- Any material financing transactions;
- Compensation received, or that may be received, by the SPAC sponsor and its affiliates and any potential dilutive impact; and
- Conflicts of interest.

For SPAC IPOs, proposed Item 1602(b) would require the following information in the prospectus summary:

- Process for identifying and evaluating a potential target;
- Whether shareholder approval of a de-SPAC transaction will be required;
- Material terms of the trust account;
- Whether the offered securities are of the same class as those held by the SPAC sponsor and its affiliates;
- Time period required to consummate a de-SPAC transaction, and the process of extending the period, consequences to the SPAC sponsor for extending, and voting or redemption rights of shareholders with respect to an extension;
- Additional financings and their impact on shareholders;
- Compensation received, or that may be received, by the SPAC sponsor and its affiliates and any potential dilutive impact, including tabular disclosure; and
- Conflicts of interest.

For de-SPAC transactions, proposed Item 1604(b) would require the following information in the prospectus summary:

- Background and material terms of the de-SPAC transaction;
- Fairness of the de-SPAC transaction;[44]
- Conflicts of interest;
- Compensation received, or that may be received, by the SPAC sponsor and its affiliates and any potential dilutive impact, including tabular disclosure;
- Financing transactions; and
- Redemption rights.

It appears the SEC's intent with the required disclosure items noted above is to standardize the information presented by SPACs in SPAC IPOs and de-SPAC transactions. Many of the required disclosures would largely codify existing market practices, and any new disclosure slated for the cover page and the prospectus summary is information that is substantively being disclosed already by the majority of SPACs elsewhere in the document, so as a practical matter compliance with the rules should not be overly burdensome. However, requiring such disclosure to be included at least three times in the document (*e.g.*, on the cover page, in the summary, and in the body of the document where the same information often appears multiple times) seems excessive and potentially distracting to investors.

Disclosure and Procedural Requirements in De-SPAC Transactions

Background of and Reasons for the De-SPAC Transaction; Terms and Effects

Proposed Item 1605 would require the following disclosure in connection with de-SPAC transactions:

- A summary of the background of the de-SPAC transaction, including a description of any contracts, negotiations or transactions that have occurred concerning the de-SPAC transaction;[45]
- Disclosure of the material terms of the de-SPAC transaction, including (1) a brief description of the de-SPAC transaction, (2) a brief description of any related financing transaction, including any payments from the SPAC sponsor to investors in connection with the financing transaction, (3) a reasonably detailed discussion of the reasons for engaging in the de-SPAC transaction and for the structure and timing of the de-SPAC transaction and any related financing transaction, (4) an explanation of any material differences in the rights of security holders of the combined company as a result of the de-SPAC transaction after its completion, (5) a brief statement as to the accounting treatment of the de-SPAC transaction, if material, and (6) the federal income tax consequences of the de-SPAC transaction, if material;[46]
- A description of the effects of the de-SPAC transaction and any related financing transaction on the SPAC and its affiliates, the SPAC sponsor and its affiliates, the target company and its affiliates and unaffiliated security holders of the SPAC, including a reasonably detailed discussion of the benefits and detriments to each of the aforementioned categories of stakeholders, which must be quantified to the extent practicable;[47]
- Disclosure of any material interests in the de-SPAC transaction or any related financing transaction held by the SPAC sponsor and the SPAC's officers and directors, including fiduciary or contractual obligations to other entities as well any interest in, or affiliation with, the target company;[48] and
- A statement on whether or not security holders are entitled to any redemption or appraisal rights and if so, a summary of such rights and if not, an outline of any other rights available to security holders.[49]

For the most part, these proposed additional disclosures are either already required by the rules governing registration statements and proxy statements or are standard industry practice (partly in response to comments received during the SEC review process).

Requirements for Tender Offers Conducted in De-SPAC Transactions

Proposed Item 1608 of Regulation S-K would require that a Schedule TO filed in connection with a de-SPAC transaction contain the same information about the target company as would be required under the proxy rules and that the procedural tender offer rules would apply. A de-SPAC transaction structured to only require a Schedule TO, as opposed to a registration statement or proxy statement, is exceedingly rare, as it would only apply when the SPAC survives and is not issuing more than 20% of its outstanding securities as equity consideration or in a PIPE. The Proposing Release indicates that the SEC believes it is merely codifying a staff position with this addition. However, as drafted Item 1608 would apply to all tender offers filed by SPACs, not merely those in connection with a de-SPAC transaction, which could slow such a tender in order to include all the additional information (and potentially clear SEC comments thereon).[50] Moreover, proposed Rule 145a would effectively require the use of Form S-4 or F-4, and thus eliminate the ability of SPACs to use merely a Schedule TO in connection with a de-SPAC transaction.

Structured Data Requirement

The SEC is proposing to require that all information disclosed in response to new Subpart 1600 of Regulation S-K be tagged in Inline XBRL. The stated purpose for the requirement is to allow for automated extraction and analysis of granular SPAC disclosures, including comparison of information on SPAC sponsor compensation and material conflicts of interest. The SEC acknowledges that this would accelerate tagging obligations for SPACs as compared to other public companies, since XBRL tagging is not required in non-SPAC IPO filings.

Aligning De-SPAC Transactions with Initial Public Offerings

In the Proposing Release, the SEC acknowledges that private operating companies have increasingly turned to de-SPAC transactions as a means of accessing public securities markets and becoming public reporting companies, and proposes a number of new rules and amendments to existing rules that the SEC claims will more closely align the treatment of private operating companies entering the public markets through de-SPAC transactions with that of companies conducting traditional IPOs.

Aligning Non-Financial Disclosures in De-SPAC Disclosure Documents

The SEC is proposing to require disclosure with respect to a target company in a de-SPAC transaction that is not subject to the reporting requirements of the Exchange Act pursuant to the following existing items of Regulation S-K:

- Item 101 (description of business);
- Item 102 (description of property);
- Item 103 (legal proceedings);
- Item 304 (changes in and disagreements with accountants and financial disclosure)
- Item 403 (security ownership of certain beneficial owners and management, assuming the completion of the de-SPAC transaction and any related financing transaction); and

- Item 701 (recent sales of unregistered securities).

These items of Regulation S-K are required by Form S-1 to be addressed in connection with an IPO and, except for Item 701, are already disclosed with respect to target companies in connection with de-SPAC transactions. Therefore, this required disclosure would largely codify existing disclosure practice in de-SPAC transactions.

Minimum Dissemination Period

The SEC is proposing to amend Exchange Act Rules 14a-6 and 14c-2, as well as to add instructions to Forms S-4 and F-4, to require that prospectuses and proxy and information statements filed in connection with de-SPAC transactions be distributed to shareholders at least 20 calendar days in advance of a shareholder meeting or the earliest date of action by consent, or the maximum period for disseminating such disclosure documents permitted under the applicable laws of the SPAC's jurisdiction of incorporation or organization if such period is less than 20 calendar days.

Under the existing regulatory framework, which is dictated by jurisdictional requirements,[51] SPACs are typically required to deliver notice of the SPAC's special meeting not less than 10 days before the meeting[52] and, if the SPAC is a Delaware entity and will be directly merging with another entity, such notice is typically required at least 20 days before the meeting.[53] This notice is included at the beginning of the SPAC's proxy statement and effectively requires that final versions of all proxy materials be delivered to the SPAC's shareholders at least 10 days (or 20 days, as applicable) before the SPAC's special meeting. However, since the jurisdictional requirements technically only apply to a "notice" rather than the full proxy materials, the SEC believes that a SPAC and its SPAC sponsor may have incentives to provide prospectuses or proxy or information statements for a de-SPAC transaction to the SPAC's security holders within an abbreviated time frame, leaving the security holders with relatively little time to review what are often complex disclosure documents for these transactions.

The SEC's proposed solution does not align with the treatment of IPOs. An IPO prospectus is substantially final at launch of the IPO roadshow. However, since there is no required length for a roadshow, investors in an IPO may only have access to a substantially final version of the prospectus for a few days prior to making their investment decision. Under the current framework, the final registration statement or proxy statement in a de-SPAC transaction is available for at least 10 days and, under the proposed new framework, at least 20 days prior to the SPAC's shareholder meeting, and a preliminary version is typically publicly available for up to several months longer than in an IPO.

The SEC justifies this differential treatment by citing the complexity of the SPAC structure, the conflicts of interest that are often present in this structure and the effects of dilution on non-redeeming shareholders, but it fails to appreciate that many of these same considerations can be present in IPO transactions and that this proposed rule is decidedly contrary to the SEC's stated intention of aligning de-SPAC transactions with IPOs.

Re-Determination of Smaller Reporting Company Status

The SEC is proposing to require a redetermination of smaller reporting company ("**SRC**") status following the consummation of a de-SPAC transaction.

A SRC is defined as a public company that has (1) a public float of less than $250 million or (2) less than $100 million in annual revenues and either no public float or a public float of less than $700 million. SRC status is determined at the time of filing an initial registration statement under the Securities Act or Exchange Act for shares of common equity and is re-determined on an annual basis. SRC status allows companies to avail themselves of reduced disclosure obligations, notably with respect to financial statements, and SRCs typically have six to 12 months to transition to standard reporting requirements after losing SRC status. A foreign private issuer is not eligible to take advantage of the reduced disclosure requirements for SRCs unless it uses the forms and rules designated for domestic issuers and provides financial statements prepared in accordance with GAAP.

Given their structure, most SPACs qualify for SRC status, and when a SPAC is the legal acquirer of the target company in a de-SPAC transaction, the post-closing company is currently permitted to retain this status until the next annual determination date. This is particularly relevant when only two years of the target company's audited financial statements are included in the Form S-4 or proxy statement filed in connection with the de-SPAC transaction. Retaining the SPAC's SRC status after closing of the de-SPAC transaction means the post-closing company would not be required to file more audited financial statements than were required in the Form S-4 or proxy statement for the de-SPAC transaction.

The proposed rules would require a redetermination of the SRC status of the post-closing company prior to the time the post-closing company makes it first SEC filing, other than the Super 8-K, with the public float threshold measured as of a date within four business days after the consummation of the de-SPAC transaction and the revenue threshold determined by using the annual revenues of the target company as of its most recently completed fiscal year. This change could be potentially problematic for transactions where the SPAC is a SRC and the legal acquirer, the target company was a SRC prior to the closing of the de-SPAC transaction and filed two years of audited financial statements and the post-closing public float exceeds $700 million.

The re-determination of the public float will be dependent on redemption levels and the post-closing trading price and could lead to significant uncertainty regarding required disclosure if the post-closing company's first annual report is due shortly after closing or the company's resale registration statement is required to be filed after the company's first periodic report. If the post-closing public float exceeds $700 million, the post-closing company would be required to include three years of audited financial statements in its annual report and any registration statement, which may be more than what was included in the S-4 or proxy statement filed in connection with the de-SPAC transaction. Notably, this uncertainty does not exist after IPOs where required financial statements are based on EGC status and the issuer is not required to file financial statements for periods prior to the earliest period included in registration statement.

Financial Statement Requirements in Business Combination Transactions Involving Shell Companies

The proposed amendments with respect to financial statement requirements in business combination transactions involving shell companies are intended to more closely align with those required in IPOs.

Number of Years of Financial Statements

Currently, a registration statement on Form S-4 or Form F-4 and a proxy or information statement requires financial statements of the target company for each of the three most recent fiscal years, except in the following scenarios where two years are permitted:

- The target company qualifies as a SRC;
- The target company would be an EGC, even if not a SRC, if it were conducting an IPO and the SPAC's first annual report has not yet been filed or been required to be filed; or
- The transaction is registered on a Form F-4 and either the target company is a first time adopter of International Financial Reporting Standards or the Form F-4 is the initial registration statement and provides for U.S. GAAP financial statements.

To align more closely with the financial statement reporting requirements of IPOs, when the registrant is a shell company and the financial statements of the predecessor to the registrant are required in a registration or proxy statement, proposed Rule 15-01(b) would provide that the registrant must file financial statements of the predecessor's business in accordance with Articles 3 and 10 of Regulation S-X or Article 8 of Regulation S-X, as applicable. An EGC shell company would then be permitted to include in such registration or proxy statement two years of statements of comprehensive income, changes in stockholders' equity and cash flows for an EGC target company, regardless of whether an annual report has been filed or been required to be filed.

Audit Requirements of the Predecessor

Proposed Rule 15-01(a) of Regulation S-X would require financial statements of the target business that is or will be the predecessor to a shell company to be audited by an independent accountant in accordance with PCAOB standards. Such target companies would then need to comply with Article 2 of Regulation S-X. This requirement would codify the SEC's existing position (which is inconsistent with the technical requirements for proxy statements and registration statements).

Age of Financial Statements of the Predecessor

Proposed Rule 15-01(c) of Regulation S-X would align the age requirements of financial statements of the predecessor of a shell company with the age requirements specified in Article 8 or Article 3 of Regulation S-X, as applicable.

The intent of this proposed rule is to further align the disclosure requirements in de-SPAC transactions with those in IPOs, including with respect to financial statement presentations, and this change would codify existing practice by SPAC market participants.

Acquisitions of Businesses by a Shell Company Registrant or Its Predecessor That Are Not or Will Not Be the Predecessor

In addition to the target company's financial statements, financial statements of acquired businesses that are not or will not be the predecessor may also be required. The existing rules only require presentation of financial statements of these other businesses if omission of such statements would render the target company's financial statements misleading.

Proposed Rule 15-01(d) of Regulation S-X would require the application of Rule 3-05 or 8-04 of Regulation S-X (*i.e.*, provisions related to acquired businesses) to other businesses that have been acquired by the target company. Further, proposed Rule 15-01(d)(2) would specify when financial statements of recently acquired businesses that are not the target company's, which are currently omitted, would be required to be filed. The existing rules allow financial statements to be omitted in registration statements for businesses that are less than 50% significant, and instead must be filed in a Form 8-K no later than 75 days after the acquisition. Due to uncertainty on how to treat those financial statements when the target company is not yet subject to Exchange Act reporting requirements, proposed Rule 15-01(d)(2) would require the omitted financial statements to be filed in an Item 2.01(f) Form 8-K filed with Form 10 information (a "**Super 8-K**").

In connection with the above, the SEC is also proposing amendments to the significance tests in Rule 1-02(w) of Regulation S-X. The amendments to Rule 1-02(w) would require significance to be calculated using the target company's financial information as the denominator instead of that of the shell company registrant.

In the event other businesses are acquired by the target company shortly before the Super 8-K is filed, the proposed rules would effectively accelerate the financial statement requirements and mandate their presentation on a faster timeline than if the business was instead acquired by an operating company.

Financial Statements of a Shell Company Registrant After the Combination

With respect to filings made after a business combination, proposed Rule 15-01(e) of Regulation S-X would allow a former SPAC to exclude financial statements of the SPAC for periods prior to the acquisition once: (1) financial statements of the [SPAC/predecessor][54] have been filed for all required periods through the acquisition date and (2) the registrant's financial statements including the period the acquisition was consummated have been filed. Such financial statements of the SPAC would be required in all filings prior to the first post-business combination periodic report.

Other Amendments

Proposed Amendment to Rule 11-01(d) of Regulation S-X

The proposed amendment to Rule 11-01(d) would define SPACs as "businesses" for purposes of the rule (*i.e.*, provisions related to the presentation requirements of pro forma financial information). This would require companies acquiring SPACs to file financial statements of the SPAC and pro forma financial statements. SPACs function similarly to a shell company with nominal to no operations and it would make little sense to qualify a SPAC as a "business" for purposes of pro forma financial presentation requirements. The SEC's stated reasoning for this proposed amendment is that financial statements of the SPAC "could" be material when they underpin adjustments to the pro forma financial statements. This information would have already been presented in the Form S-4 or Form F-4, so there is not much reason to require it again.

Proposed Amendment to Item 2.01(f) of Form 8-K

The proposed amendment to Item 2.01(f) of Form 8-K would revise the item to refer to the "acquired business" rather than the "registrant," as currently stated in the Form, as part of the discussion of what information is required to be included in a Super 8-K. The SEC's intent with this amendment is to "eliminate any potential misunderstanding as to the entity for which Item 2.01(f) disclosure is necessary"[55] and clarify the provided information should relate to the acquired business and for periods prior to consummation of the acquisition and not the shell company registrant.

Proposed Amendments to Rules 3-01, 8-02, and 10-01(a)(1) of Regulation S-X

Proposed amendments to Rules 3-01, 8-02, and 10-01(a)(1) would specifically require the presentation of balance sheets and statements of comprehensive income for both the registrant and the predecessor, rather than only statements of comprehensive income for both the registrant and the predecessor as required under the current rules.

We believe this proposed rule will have minimal impact on disclosure and correlated costs since many companies already include both balance sheets and statements of comprehensive income in their financial statements.

Other Potential Revisions

In addition to the proposed rules, the SEC requested feedback on a number of other topics, as well as encouraging comments on other aspects of the proposals and suggestions for additional changes.

One request discusses the "empty voting" phenomenon, where SPAC shareholders can vote against a de-SPAC transaction and still exercise redemption rights. Most SPACs permit such decoupling of the vote from continued ownership in the company. We think concerns over empty voting are overstated, as the individual redemption right of each shareholder makes the vote a mere formality. More importantly, the current system of proxy solicitation in the U.S. (requiring a record date, mailing, and the proposed minimum dissemination period) both (a) already introduces a risk of empty voting in all public company mergers and (b) means that purchasers of SPAC shares after the record date for the vote do not have the right to vote for or against the transaction. If SPAC shareholders were required to vote "no" on the transaction in order to have redemption rights (which is permissible under the exchange listing rules), any purchaser of shares after the record date would have irredeemable shares. To the extent aligning the de-SPAC process with the traditional IPO process is desired, there is no requirement in an IPO for there to be a vote among the offerees, and no minimum percentage acceptance by offerees in order to proceed with the offering.

The SEC notes that former shell companies, including SPACs, are subject to different (and worse) treatment under a variety of existing rules.[56] Most of these rules were adopted in the early 2000s, when SPACs were not exchange listed, out of concern over pump-and-dump schemes relating to transactions with limited prompt disclosure. Many of the concerns do not apply to exchange-listed SPACs due to the need for a proxy solicitation in almost every de-SPAC transaction, and the proposed rules would even further mitigate the concerns that motivated the shell company regulations. Accordingly, the SEC should eliminate the different treatment for companies going public via de-SPAC transactions.

Comment Process and Importance; Final Rules

The SEC will accept written comments from members of the public through May 31, 2022, unless they extend the deadline for comments. These comments will form part of the "administrative record" that serves as the basis for the SEC's decision to issue any final rule. Filing comments is an important way to raise specific concerns with the proposal or to provide support for aspects of the proposal. The SEC is required to review and consider these comments before finalizing a rule, and comments can result in changes to a proposal. Even when the comments do not result in changes to a rule, they are important because of the role they play in legal challenges to any final rule. Comment letters are part of the body of evidence (*i.e.*, the "**administrative record**") that a court will consider when evaluating the SEC's decision, and courts generally will not allow an argument to be raised in court unless it was already raised in a public comment. Providing information that supports or critiques the SEC's proposal can therefore play an important role in whether a court ultimately upholds the SEC's rule.

We anticipate that the SEC will receive a substantial number of comments, such that adopting final rules may be delayed as the SEC processes such comments in a final rule release. It is also possible the SEC may bifurcate rule-making between hotly contested and relatively benign proposals.

We expect to see final rules adopted this year. Any final rule will include an "effective date" that will trigger the rule's requirements. Court challenges on particularly controversial proposals may be filed as soon as the SEC issues any final rule and may impact the effective date of the rule because courts have the power to "stay" or pause a rule's effective date during the case or once the case is completed.

[1] Such a defense requires the defendant to essentially establish that it believed the challenged disclosure was true and did not contain any material omissions, it had reasonable grounds for that belief, and it undertook a reasonable investigation into the accuracy of the challenged disclosure.

[2] Proposing Release, p. 95.

[3] "Disclosure" in connection with a de-SPAC transaction may include a proxy statement, a registration statement on Form S-4 or F-4, a prospectus included in a registration statement, or a tender offer statement on Schedule TO. By virtue of proposed Rule 145a, almost all de-SPAC transactions would require a registration statement, which will contain a joint proxy statement and prospectus.

[4] Section 2(a)(11) of the Securities Act (defining "underwriter").

[5] Proposing Release, p. 97.

[6] *Id*.

[7] Proposing Release, p. 98. We view the SEC's reference to PIPE investors potentially being deemed as statutory underwriters as being limited to "purchasing 'with a view to' distribution," rather than a suggestion that purchasing securities in a PIPE for investment purposes could be "participating" in the SEC's conceptual distribution of securities to the SPAC investors.

[8] *Pinter v. Dahl*, 486 U.S. 622 (1988).

[9] *In re Lehman Brothers Mortgage-Backed Securities Litigation*, U.S. Court of Appeals, Second Circuit, Fed. Sec. L. Rep. ¶96,310, 650 F.3d 167, (May 11, 2011).

[10] *Id*.

[11] Proposing Release p. 91, citing Harold S. Bloomenthal & Samuel Wolff, Due diligence defenses – Underwriter's responsibilities and liabilities, 3B Sec. & Fed. Corp. Law (2d. Ed.) and *New High Risk Ventures*, Release No. 33-5272 (July 27, 1992).

[12] Proposing Release, pp. 91 and 92, citing *In the matter of the Richmond Corp.,* Release No. 33-4584 (Feb. 27, 1963).

[13] Proposing Release, note 18, at p. 92.

[14] For example, NYSE and NASDAQ exchange listing rules require a third-party valuation be conducted by a financial advisor for direct listings. Whether the financial advisor was a statutory underwriter due to its participation was a point of debate among the SEC commissioners in approving the NYSE primary direct listing proposal in 2020, with two of the commissioners (Allison Herren Lee and Caroline A. Crenshaw, who voted in favor of the proposed SPAC rules) dissenting on the ground that the SEC did not "provid[e] guidance addressing what might trigger status as a statutory underwriter for other market participants involved in a primary direct listing". *See* https://www.sec.gov/news/public-statement/lee-crenshaw-listings-2020-12-23.

[15] In de-SPAC transactions where a new registrant is formed, or the target company acquires the SPAC, it is unclear under the current rule whether the PSLRA exclusion for IPOs would apply.

[16] *Iowa Pub. Emps.' Ret. Sys. v. MF Global, Ltd.*, 620 F.3d 137, 141 (2d Cir. 2010).

[17] We note the following statement in the Proposing Release: ". . . projections are almost never provided to the public in connection with an IPO . . . ." Proposing Release, p. 248.

[18] Item 1014(a) of Regulation M-A; Proposed Item 1606(a).

[19] Proposing Release, pp. 195 and 228. The SEC estimates the average cost of a fairness opinion for a de-SPAC transaction at $270,000.

[20] Proposed Item 1607(a).

[21] Form S-4, Item 4.b.; Form F-4, Item 4.b.; Schedule 14A, Item 14(b)(6).

[22] With respect to proposed Item 1607(b), a substantive deviation from Item 1015(b) of Regulation M-A is the addition of "the valuation of the target company" in Item 1607(b)(5).

[23] Proposing Release, p. 136.

[24] Rule 2a-7(a)(14) defines "Government Money Market Fund" as "a money market fund that invests 99.5 percent or more of its total assets in cash, government securities, and/or repurchase agreements that are collateralized fully."

[25] Proposed Rule 3a-10.

[26] "Government securities", as used in proposed Rule 3a-10, is limited to U.S. government securities.

[27] Rule 2a-7(d) imposes conditions relating to portfolio maturity, portfolio quality, portfolio diversification and portfolio liquidity.

[28] Technically, the 18-month period begins with the effectiveness of the IPO registration statement, which may pre-date the IPO pricing date and will pre-date the IPO closing date.

[29] Proposing Release, p. 271.

[30] Proposing Release, p. 265.

[31] For example, Rule 3a-8 permits R&D companies, subject to a number of conditions, to invest their cash in securities indefinitely. Similarly, the SEC has granted exemptive orders for companies with substantial cash investments in securities and low income from operations that are substantially longer than the proposed deadlines, or are indefinite (*see*, *e.g.*, *In re Snowflake, Inc.,* https://www.sec.gov/rules/ic/2020/ic-34085.pdf; *In re Lyft, Inc.*, https://www.sec.gov/rules/ic/2019/ic-33442.pdf; and *In re Upstart Holdings, Inc.,* https://www.sec.gov/rules/ic/2020/ic-34124.pdf). In one instance, a court concluded that a company that held a majority of its assets in securities for a decade was not primarily engaged in the business of investing in securities (*SEC v. National Presto Industries, Inc.*, 486 F.3d 305, 315 (7th Cir. 2007)).

[32] Proposing Release, p. 156.

[33] For a more thorough discussion, see https://corpgov.law.harvard.edu/2021/09/03/special-purpose-acquisition-companies-and-the-investment-company-act-of-1940/ .

[34] *Wilson v. Great Am. Indus., Inc.* 855 F.2d 987, 995 (2d Cir. 1988).

[35] Proposing Release, p. 104.

[36] In rare circumstances the target company itself is the registrant.

[37] *See In re Weight Watchers Int'l Inc. Sec. Litig.*, 504 F. Supp. 3d 224, 262–63 (S.D.N.Y. 2020).

[38] *Matrixx Initiatives, Inc. v. Siracusano*, 563 U.S. 27, 48 (2011).

[39] *Set Cap. LLC v. Credit Suisse Grp. AG*, 996 F.3d 64, 84 (2d Cir. 2021).

[40] Proposed Item 1601.

[41] Moreover, the use of the term SPAC in proposed Rule 3a-10 under the Investment Company Act of 1940 suggests that a company continues to be a "SPAC" even after completion of a de-SPAC transaction.

[42] Arguably, this is the only prong that picks up most "SPAC sponsors," and is not pertinent for the stated reasons for the disclosure that would be required by the proposed rules.

[43] Proposed Items 1602(a)(4), 1602(c), and 1604(c).

[44] *See* discussion of proposed Item 1606 under "Fairness Disclosure" above.

[45] Proposed Item 1605(a).

[46] Proposed Item 1605(b).

[47] Proposed Item 1605(c).

[48] Proposed Item 1605(d).

[49] Proposed Item 1605(e).

[50] Some SPACs are required by their constituent documents to tender for their warrants in connection with extensions of outside dates.

[51] Beyond Rule 14a-16 of the Exchange Act that permits using the notice and access method of proxy delivery, SEC rules do not require a specific amount of time for allowing stockholders to consider and vote upon new proposals. Section 401.03 of the NYSE's Listed Company Manual "recommends" but does not require at least 30 days between the record and meeting dates for a meeting to give ample time for the solicitation of proxies.

[52] DGCL 222(b). Article 61 of The Cayman Companies Act requires at least five days notice of meetings, but most Cayman SPAC governing documents align with the Delaware requirements and require 10 days notice of meetings.

[53] DGCL 251(c).

[54] In the Proposing Release, the description of the rule uses the term "shell company," while the text of proposed Rule 15-01(e) uses the term "predecessor."

[55] Proposing Release, p. 261.

[56] For example, Rule 144 is not available for resale of securities of former shell companies to the same extent as for securities issued by companies that go public via traditional IPO, former shell companies are limited in their ability to use Form S-8 for equity compensation and former shell companies are "ineligible issuers" for purposes of using free-writing prospectuses or qualifying as well-known seasoned issuers for three years post de-SPAC transaction.

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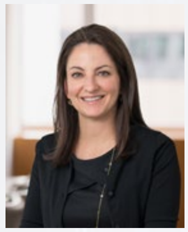

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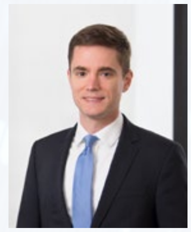

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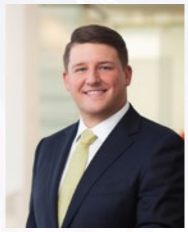

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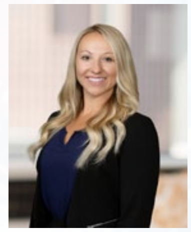

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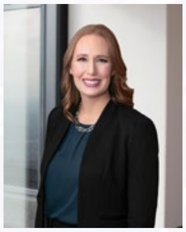

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