Cahill

April 15, 2022

SEC Proposes New Rules and Amendments Relating to SPACs

On March 30, 2022, the Securities and Exchange Commission ("SEC") proposed new rules and amendments relating to special purpose acquisition companies ("SPACs"). Since 2020, the U.S. securities markets have experienced an unprecedented surge in initial public offerings ("IPOs") of SPACs.[1] In the wake of this boom, some commentators have expressed concerns about, among other things, various aspects of the SPAC structure, as well as the adequacy of the disclosures provided to investors in SPAC transactions as compared to traditional IPOs.[2] In response to such concerns, the SEC's proposal aims to (i) enhance existing disclosure requirements and investor protections in SPAC IPOs and subsequent business combinations with private operating companies (so-called "de-SPAC transactions"); (ii) address the treatment under the Securities Act of 1933 (the "Securities Act") of business combination transactions involving shell companies generally; (iii) update previous guidance on the use of projections in SEC filings; and (iv) assist SPACs in assessing when they may be subject to regulation under the Investment Company Act of 1940 (the "Investment Company Act").

I. Proposed New Subpart 1600 of Regulation S-K

The SEC proposes to add a new Subpart 1600 to Regulation S-K setting forth additional disclosure requirements applicable to SPACs regarding the sponsor, potential conflicts of interest, and dilution, as well as requiring certain disclosures on the prospectus cover page and in the prospectus summary.

- Proposed Item 1603(a) would require a SPAC to disclose detailed information on how the rights and interests of the sponsor, its affiliates, and any promoters may differ from, and may conflict with, those of public shareholders.
- Proposed Item 1603(b) would require disclosure of any actual or potential material conflicts of interest between (1) the sponsor or its affiliates or the SPAC's officers, directors, or promoters, and (2) unaffiliated security holders.
- Proposed Item 1603(c) would require disclosure regarding the fiduciary duties each officer and director of a SPAC owes to other companies.
- Proposed Items 1602(a)(4), 1602(c) and 1604(c) would require additional disclosure about the potential for dilution in all registered offerings by a SPAC and all de-SPAC transactions.
- Proposed Item 1602 would require that certain disclosures be highlighted on the prospectus cover page and in the prospectus summary, such as the time frame for the SPAC to consummate a de-SPAC transaction, sponsor compensation, dilution (including simplified tabular disclosure), and conflicts of interest.

[1] SPACInsider, SPAC IPO Transactions: Summary by Year, *available at* https://spacinsider.com/stats/ (last visited Apr. 7, 2022).

[2] *See*, *e.g.*, John Coates, *SPACs, IPOs and Liability Risk under the Securities Laws*, *available at* https://www.sec.gov/news/public-statement/spacs-ipos-liability-risk-under-securities-laws.

Proposed Subpart 1600 of Regulation S-K also would require enhanced disclosure for de-SPAC transactions. In particular, the proposed rules would require a statement from the SPAC as to whether it reasonably believes that the de-SPAC transaction and any related financing transaction are fair to unaffiliated security holders, and a discussion of the basis for this statement, including whether the SPAC has received any fairness-related third party report, opinion, or appraisal. In practice, this new requirement is likely to increase the instances in which a SPAC board will obtain a third party fairness opinion.

II. Proposals to Align De-SPAC Transactions with IPOs

The SEC also proposes a number of new rules and amendments to align more closely the treatment of private operating companies entering the public markets through de-SPAC transactions with that of companies conducting traditional IPOs. For example, the SEC proposes to amend Form S-4 and Form F-4 to require that the SPAC and the target company be treated as co-registrants with respect to such filings, resulting in the target company being subject to the signature requirements of the form and therefore liable under Section 11 of the Securities Act for any material misstatements or omissions therein. In addition, the SEC proposes to require a re-determination of smaller reporting company status following the consummation of a de-SPAC transaction. The SEC also proposes amendments that would make the statutory safe harbor in the Private Securities Litigation Reform Act of 1995 unavailable for forward-looking statements, such as projections, made in connection with de-SPAC transactions.

Finally, proposed Rule 140a would clarify that a person who has acted as an underwriter in a SPAC IPO and participates in the distribution by taking steps to facilitate the de-SPAC transaction, or any related financing transaction, or otherwise participates (directly or indirectly) in the de-SPAC transaction will be deemed to be an "underwriter" within the meaning of Section 2(a)(11) of the Securities Act. If Rule 140a is adopted as proposed, we anticipate that investment banks working on de-SPAC transactions will insist on performing detailed legal documentary due diligence review on the target, and obtaining legal opinions on the target's disclosures and a comfort letter from the target's auditor, consistent with a traditional IPO.

III. Business Combinations Involving Shell Companies

The SEC also proposes new rules that would apply to business combination transactions involving shell companies, including but not limited to de-SPAC transactions. First, under proposed new Rule 145a under the Securities Act, such transactions would be deemed to involve a sale of securities to a reporting shell company's shareholders within the meaning of Section 2(a)(3) of the Securities Act.[3] Second, pursuant to new Article 15 of Regulation S-X and related amendments, the required financial statements of private operating companies in connection with such transactions would be more closely aligned with those required in registration statements on Form S-1 or Form F-1 for an IPO.

IV. Projections Disclosure

The SEC also proposes to amend Item 10(b) of Regulation S-K to expand and update the SEC's guidance on the use of projections. Among other things, the proposed amendments would require any projected measures that are not based on historical financial results or operational history to be clearly distinguished from projected measures that are based on historical financial results or operational history. The proposed amendments also would clarify that

[3] The SEC emphasizes that business combinations between two *bona fide* non-shell entities, as well as the business combination of one shell company into another shell company, would be excluded from the scope of the new rule.

Item 10(b)'s guidance applies to projections of future economic performance of persons other than the registrant, such as the target company in a business combination.

In addition, given the widespread use of projections in de-SPAC transactions, the SEC also proposes new Item 1609 of Regulation S-K that would set forth additional disclosure requirements on financial projections used in de-SPAC transactions. New Item 1609 would require a de-SPAC registrant to disclose: (i) the purpose for which any projections were prepared and the party that prepared them; (ii) all material basis and assumptions underlying the projections, and any factors that may materially impact such assumptions; and (iii) whether the disclosed projections still reflect the view of the board or management of the SPAC or target company, as applicable, as of the date of the filing.

V. Status of SPACs under the Investment Company Act

Lastly, the SEC proposes new Rule 3a-10 under the Investment Company Act, which would provide a safe harbor from the definition of "investment company" under Section 3(a)(1)(A) of the Investment Company Act for SPACs that meet certain conditions that limit their duration, asset composition, business purpose and activities. For example, to rely on the safe harbor, a SPAC would have to file a report on Form 8-K announcing that it has entered into an agreement with a target to engage in a de-SPAC transaction no later than 18 months after the effective date of the SPAC's IPO registration statement. The SPAC then would have to complete the de-SPAC transaction no later than 24 months after the effective date of its IPO registration statement.

VI. Conclusion

The proposed new rules and amendments, if adopted as proposed, would impose significant new disclosure obligations on both SPACs and target companies in de-SPAC transactions and certain other market participants in business combinations and in connection with the disclosure of projections.

The public comment period will remain open for 60 days following publication of the proposing release on the SEC's website (*i.e.*, until May 31, 2022) or 30 days following publication of the proposing release in the *Federal Register*, whichever period is longer.

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If you have any questions about the issues addressed in this memorandum, or if you would like a copy of any of the materials mentioned in it, please do not hesitate to call or email authors Geoffrey E. Liebmann (partner) at 212.701.3313 or gliebmann@cahill.com; Sarah Klein-Cloud (attorney) at 212.701.3231 or sklein-cloud@cahill.com; or email publications@cahill.com.