

The New SEC SPAC Rules: Sufficient to Protect Investors?

SPACs have become a very popular investment vehicle. In many respects they are the vehicle of choice for IPOs these days. One of the reasons SPACs may popular – perhaps the IPO vehicle of choice – is their simplicity compared to the traditional IPO which often has a lengthy and complex set of offering papers that are costly to assemble.

At the same time regulators such as SEC Chair Gensler have repeatedly cautioned that simplicity comes at a price. SPACS often come with little disclosure, potential conflicts of interests and significant risks, particularly for main street investors who may not see the potential for loss lurking behind a name that sounds like the investment is tied to a crypto asset or some gamified investment opportunity just too good to passed up.

The Commission has proposed new rules to govern SPACs, focused on investor protection. The proposals include a mix of provisions which would enhance disclosure regarding the SPAC and its sponsor and conflicts and the de-SPAC deals while adding sections which would increase accountability. The proposals would:

1. Add disclosures about SPAC sponsors, conflicts of interests and the potential dilution of investor interest;
2. Those who are underwriters of the original transaction would also be deemed to be underwrites in any de-SPAC transaction under the proposals, adding accountability to the deals;
3. Another proposal centers on business combinations involving a reporting shell company and another entity not a shell company which, under the proposals, would be considered a sale of securities to the reporting shell company shareholders for purposes of the Securities Act, again adding accountability;
4. There will be a better alignment of the financial statements of private firms in transactions involving shell companies with those required in registration statements for IPOs under the proposals;
5. The proposals also seek to increase the reliability of projections and give investors a better opportunity to evaluate the projections by enhancing disclosure of the underlying basis for the projections; and
6. SPACs will not be deemed Investment Companies under the 1940 Act (or inadvertent

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investment companies) by complying with certain conditions which include: a) maintaining assets comprised only of cash, government securities and certain money market funds; b) seeking to complete a de-SPAC deal after which the surviving entity will be primarily engaged in the business of the target firm; and c) entering into an agreement with a target company to engage in a de-SPAC transaction within 18 months after its initial IPO and complete its initial public offering and de-SPAC deal within 24 months.

Overall, the proposed rules would enhance the disclosures for investors and perhaps the overall fairness of de-SPAC deals. While the basket of proposals will improve the overall investor protections, they will still in fact be added to a blank check company controlled by the sponsors. Whether the proposals will furnish investors sufficient information to actually evaluate the transactions is at best unclear. Stated differently, is disclosure enough here to effectively protect main street investor? Doubtful at best.