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# SPAC regulation could require more disclosure rules

*The SEC has issued guidance on the booming SPAC market, and many believe that more regulation is coming. Will regulators step in before the market shows signs of collapse?*

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The Securities and Exchange Commission has started to address the SPAC craze, as regulators have issued new statements detailing requirements and restrictions for participants in the booming industry.

But even as the market for SPACs begin to cool off, many believe further regulation is on the way.

The SEC first addressed the recent surge in SPAC activity as **guidance** reminding participants to "clearly" disclose potential conflicts in launching an IPO or considering a merger. Last week, the SEC issued further **guidance** reminding participants that SPACs are subject to shell company regulations; must abide by Exchange Act books, records and internal control rules; and when a SPAC is listed on a national exchange, the company must satisfy initial listing standards.

These warnings, coupled with the recent **lengthy statement** from John Coates, acting director of the corporate finance division, highlight a market segment that is, especially under a Democratically-controlled Congress, ripe for more regulation.

"The SEC never liked blank check companies," Rick Frimmer, shareholder at law firm Stradling Yocca Carlson & Rauth told *Venture Capital Journal*, as these types of companies were risky and highly-regulated.

The very idea of a blank check company, where investors put money in and sponsors choose a target, is contrary to the usual disclosure rules, but they aren't in the business of steering right from wrong.

"The SEC's job is to regulate disclosures," Frimmer said. "It doesn't evaluate the merits of any particular offering."

It therefore makes sense that the SEC would want to regulate disclosures on SPACs, and according to law firm Wilmer Hale in a blog post last month, the regulator will want to know even more about potential conflicts of interest.

"The most significant enforcement risk arises from allegations of inadequate disclosures, with SPAC sponsors on the front line," the firm's post said. "The sponsor is expected to provide full and fair disclosure regarding potential risks, conflicts of interest and other material facts related to each proposed transaction."

This would include disclosures made during the IPO process in the proxy and registration statements, which outline the initial business combination. But it might take signs that the market is starting to fall apart before the Commission steps in with its full regulatory muscle.

"If enough of these [SPACs] collapse, then the SEC might tighten the rules and require, for instance, that X percent of the funds initially raised have to be committed to an identifiable investment," Frimmer said. "That could be something they would do."

### Making sense of de-SPACing

The idea of needing to identify an investment target is already causing some anxiety in the market, and the SEC is likely to scrutinize whether the risks of non-performance have been adequately identified, according to Wilmer Hale. Regulation geared at identifying an investment target early could ease this burden, but the SEC seems more concerned about other aspects of the de-SPACing.

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Since a de-SPAC deal, where a target company is chosen to take public, is technically a merger, it can issue financial forecasts that are protected like a typical M&A transaction. Traditional IPOs are unable to provide such forward-looking statements, and the SEC believes these projections to be "untested, speculative, misleading or even fraudulent," the Coates statement said.

But Coates goes further to suggest a reconsideration of how securities laws apply to SPACs, which has the potential to rupture the blank-check business model.

"If we do not treat the de-SPAC transaction as the 'real IPO,' our attention may be focused on the wrong place, and potentially problematic forward-looking information may be disseminated without appropriate safeguards," Coates said.

SPAC owners should thus prepare for such statements to be heavily scrutinized.

The other option is the Commission employs a wait-and-see approach, according to Frimmer.

Part of the draw of the SPAC market is that retail investors can access these illiquid investments. But no one wants these investments without the top-tier returns they're famous for.

"If the investing public sees that the majority of the SPACs are not returning dollars on investment, they won't invest in it," Frimmer said.

For the time being, the SPAC market appears to be slowing down despite their popularity, as numerous SPAC shares are now trading for less than their per-share trust value. That drop comes even though in the first quarter, SPACs raised more than the $83.4 billion they raised in all of 2020, according to industry tracker SPAC Research. In 2019, less than $14 billion were raised through SPACs.

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"One of the places where I think we're going to get more regulation is in the SPAC market," Scott Minerd, global chief investment officer at Guggenheim Partners told ***Bloomberg*** this week.

"If you look at the earnings estimates that are provided on the SPAC combinations or de-SPACing as its referred to, the actual delivery on those estimates has been dismal relative to what the sponsors have advertised."

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