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**Submitted by SEC Webform (http://www.sec.gov/rules/submitcomments.htm)**

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

**RE: File No. S7-13-22: Special Purpose Acquisition Companies, Shell Companies, and Projections**

Dear Ms. Countryman:

On behalf of the North American Securities Administrators Association, Inc. ("NASAA"),[1] I am writing in response to U.S. Securities and Exchange Commission ("SEC" or the "Commission") Release No. 33-11048, *Special Purpose Acquisition Companies, Shell Companies, and Projections* (the "Proposal").[2] NASAA generally supports the Proposal and believes it will provide meaningful investor protections in the Special Purpose Acquisition Company ("SPAC") initial public offering ("IPO") and De-SPAC processes. We offer the following comments both in support of the Proposal and for the Commission's consideration.

## I. Introduction

The Proposal describes how SPAC IPOs ballooned significantly in 2020 and 2021 to eclipse standard public offerings, raising more than $270 billion in the public market.[3] The registration process provides significant benefits to investors and is critical to maintaining the reputation of our capital markets. Therefore, NASAA generally supports measures designed to encourage companies to bring their securities to the public market through registered offerings.

[1] Organized in 1919, NASAA is the oldest international organization devoted to investor protection. NASAA's membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico, and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

[2] The Proposal is available at https://www.sec.gov/rules/proposed/2022/33-11048.pdf.

[3] *See* Proposal at 8. *See also* Commissioner Caroline A. Crenshaw, *Statement on the SPACs Proposal* (Mar. 30, 2022), https://www.sec.gov/news/statement/crenshaw-spac-20220330; Commissioner Allison Herren Lee, *Statement on the Proposal to Enhance Investor Protections in SPACs* (Mar. 30, 2022), https://www.sec.gov/news/speech/lee-statement-spac-proposal-033022.

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We believe that the public market offers greater transparency and opportunities for investors to review corporate disclosures and make informed decisions compared to the private markets. We also believe that the liquidity of the public market is superior and therefore is of greater benefit to issuers. However, the price of entry into the public market is robust public disclosure and greater potential liability for offering misstatements or omissions. These protections have been carefully crafted, and NASAA takes the position that regardless of the instrument used to go public (IPO, SPAC, or blank check company subject to Rule 419 under the Securities Act of 1933), similar rules for investor protection should apply. The Proposal as drafted would accomplish this goal.

## II. Disclosure Proposals

NASAA supports the Proposal's provisions for additional disclosures during the SPAC and de-SPAC process.[4] Providing more information about a sponsor's experience in the capital markets and the SPAC process would allow investors to understand the managing parties with whom they are dealing, and in particular the ability of such parties to find appropriate private target companies and craft successful post-merger businesses. We note that many SPACs already provide this information.[5] Requiring disclosures concerning the essential persons responsible for managing SPACs would have the added benefit of allowing investors to make direct comparisons when considering multiple SPAC investment opportunities. Likewise, the disclosures under consideration for potential or actual conflicts of interest, as well as for lock-up agreements for sponsors and affiliates,[6] would equip investors with the ability to evaluate concerning circumstances and withdraw from a SPAC at the redemption stage.[7]

NASAA believes that some of the most important de-SPAC disclosures proposed are those concerning the potential for dilution and the potential impacts to returns from sponsor compensation, "promote" shares, underwriting fees and warrants.[8] The unique combination of shares and warrants typical of SPAC offerings provides incentives for initial investors to trade or redeem shares as soon as possible.[9] In a de-SPAC transaction, a large portion of the cost is carried by non-redeeming shareholders.[10] For this reason, the actual net cash per share for non-redeeming

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[4] *See* Proposal, Sections II & III.

[5] Steven Kurutz, *Anyone Who's Anyone Has a SPAC Right Now*, The New York Times (Feb. 27, 2021).

[6] *See* Proposal at 32, Question 12.

[7] In our view, redemption rights are the most important investor protection feature in SPACs. However, this feature is only as good as the quality of information provided to the investor. *See* CFA Institute, *The New Age of Special Purpose Acquisition Companies, What Investors Should Know* (Mar. 2022) at 19 (the "CFA Institute Report"), https://www.cfainstitute.org/-/media/documents/article/position-paper/cfa-spac-investors.pdf.

[8] *See* Proposal, Section II.D.

[9] *See* CFA Institute Report at 24 ("most of the SPAC's initial IPO investors have an investment strategy to redeem their shares at the earliest opportunity while keeping their warrants to retain a free option on the upside potential of the postmerger company. As a result, these investors are attracted to those SPACs that allow for earlier redemption times, so the investors can get a more expedient return of capital.").

[10] Michael Klausner, Michael Ohlrogge & Emily Ruan, *A Sober Look at SPACs*, 39 Yale J. on Reg. 228 (2022).

shareholders under different redemption scenarios should be displayed in an easily understandable, tabular format, as the Commission is considering.[11] This disclosure should also provide, in the same format, the break-even points for non-redeeming investors under different scenarios, the break-even point for the sponsor, the ownership distribution for non-redeeming investors, the effects of outstanding warrants and sponsor shares, and the resulting ownership of the target company for non-redeeming shareholders and alternative investors.[12] The intricacy of this information attests to the complex nature of SPAC offerings and the necessity of robust disclosure.

Another key disclosure for investor decision-making would be the proposed fairness statement.[13] Sponsors face a number of conflicts of interest, and perhaps most pressing is the no-deal liquidation scenario if a target company is not identified, or a de-SPAC transaction is not completed. With misaligned incentives and a lower break-even point, some sponsors may be inclined to chase sub-optimal targets to complete any deal, no matter how inappropriate the post-merger business might be in terms of generating lasting shareholder value. In the current market, given the proliferation of SPAC transactions in recent years, there may be relatively few attractive options for private company targets left. NASAA therefore suggests that a third-party fairness opinion should be a required component of the fairness statement. If such an opinion concludes that the transaction is favorable for investors, redemption rates are likely to remain low and the de-SPAC transaction will mostly likely proceed. If the opinion raises concerns for investors, however, the sponsors would need to disclose why they disagree with the opinion and what factors determined their willingness to pursue the transaction regardless of the opinion. Either way, the transaction would be less likely to reach minimum cash conditions without substantial assistance from private investment in public equity ("PIPE") investors or target company private equity, and investor redemption rates would be high. Overall, if the proposed changes – including a requirement to obtain a third-party fairness opinion – enabled investors to perform these sorts of analyses, and thereby make informed redemption choices, the Proposal would benefit investor protection.

Additional disclosures surrounding de-SPAC transactions may also benefit investors. While the terms of PIPE transactions are not required to be disclosed, NASAA believes the Proposal should be expanded to require disclosure of any "sweeteners," such as sponsor shares sold to secondary investors.[14] Similarly, any lock-up periods or earnout provisions for sponsors or underwriters would be of significant interest to investors and should be required if part of the SPAC offering. Finally, we believe that the disclosure requirements should be expanded to include a sponsor's post de-SPAC selling of their holdings and the number of shares the sponsor sells.

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[11] *See* Proposal at 40, Question 20. One study showed an average 50.4% dilution at the de-SPAC stage. While some ownership dilution occurs in a traditional IPO, a reasonable investor would likely want to know that their initial $10.00 investment would have a net cash per share value of $4.60 in a typical de-SPAC transaction.

[12] This latter term includes PIPE investors, any investor(s) with non-redemption agreements, and any forward-purchase agreements entered into by the sponsor.

[13] *See* Proposal, Section II.F.2.

[14] *See* CFA Institute Report at 42. Sponsor shares transferred to PIPE investors do not necessarily dilute investor interests. However, these transfers may be of interest for sponsor participation and an investor's overall decision making.

This reporting could be time limited, for example to two years following the merger, but we believe investors would be very interested to know whether a SPAC sponsor sold all or substantially all of its position in the new entity.

## III. Section 11 Liability Proposals

NASAA supports the proposed steps to expand underwriter and issuer liability. Reaffirming Section 11 liability[15] would ensure that the underwriter either fulfills its obligations as a gatekeeper for de-SPAC target companies or sufficiently separates itself from the de-SPAC process. Likewise, the proposed co-registrant requirements, and attendant liabilities for misstatements or omissions, would ensure that target company directors, boards and managements make accurate representations regarding the status of the pre-merger entity.

We agree with the Commission's views in noting that underwriters serve a vital role in the traditional IPO process by acting as gatekeepers for companies planning to go public.[16] Underwriters receive significant compensation for their efforts, along with potential liability for misstatements and omissions. The Second Circuit Court of Appeals stated it well when it noted that, "[p]rospective investors look to the underwriter -- a fact well known to all concerned and especially to the underwriter -- to pass on the soundness of the security and the correctness of the registration statement and the prospectus.[17]" Investors and the market rely on underwriters to perform due diligence on a company entering the public market and attest to the company's viability, prospects and ability to remain a going concern. The same rules and due diligence requirements should apply in the SPAC context. Underwriters performing significant tasks to further a de-SPAC transaction should be required to meet the same standards for due diligence as in a traditional IPO.

Target company managers and directors are responsible for providing the information necessary for investor approval of a de-SPAC merger, and must provide accounting information as well as current operations and forecasts. These managers and directors also profit significantly from selling private shares and/or receiving significant ownership positions in the post-SPAC entity. With this in mind, NASAA supports the attachment of Section 11 responsibilities to the managers and directors of target companies. For higher quality private companies looking to go public, the potential for liability should not present a hurdle to participating in the public market. For entities that may not be ready to make the transition to the public market through the de-SPAC process or otherwise, this new requirement would serve to prevent such entities from coming to market until they are better prepared to do so.

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[15] 15 U.S.C. § 77k(a)(5).

[16] *See* Proposal at 90.

[17] *Chris-Craft Industries, Inc., v. Piper Aircraft Corporation*, 480 F.2d 341 (2d Cir. 1973), cert. denied, 414 U.S. 910 (1973).

## IV. Forward Looking Statements and Projections Proposals

NASAA supports the proposed changes to the definition of blank check company for purposes of the Private Securities Litigation Reform Act.[18] We see no reason why de-SPAC transactions should be treated differently than penny stock issuers or traditional IPO participants with respect to forward looking statements. As for the proposed amendments to Regulation S-K on the use of projections, we believe not only that non-GAAP metrics need to be conspicuously highlighted and marked for investor review, but also that disclosures should state succinctly that issuers with no historical operations or completed negotiations for company/asset acquisitions do not have a reasonable basis for projections.[19] Such disclosures are necessary for investors to note that projections and forward looking statements have the potential to mislead investors with creative writing, unattainable ambitions, and unreliable information on upside advantages that may have no basis in reality.

As written, the Proposal would leave the door open for projections for which there are little to no reasonable basis, when an issuer has no historical operations, and when the company or asset acquisition is speculative in nature without any disclosure.[20] The misuse of projections and forward looking statements is unfortunately a frequent feature of fraudulent exempt offerings.[21] Sponsors, target companies and underwriters that would become liable under the Proposal may attempt to evade liability by combining boilerplate risk factors with forward looking cautionary information that prefaces claims of unreasonable upside potential to investors. Though all investors hope to find the next unicorn investment opportunity, the reality is that there are far more SPACs in the market today than there are potentially desirable private company targets. The Commission should adopt stringent restrictions on projections to prevent their misuse.

## V. Investment Company Act Proposals

In general, NASAA supports the Investment Company Act safe harbor rules laid out in the Proposal.[22] We do, however, view the time horizon as proposed to potentially be burdensome on SPAC sponsors. With oversaturation in the current market, anything with strict time limits including 18 months to identify a target and 24 months to close a merger may produce sub-optimal

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18 *See id.* at 84.

19 If this change is not included in the final rule, to the extent that the SEC decides to continue to allow the publication of projections without a reasonable basis, NASAA maintains that the use of any non-GAAP financial statements or related measures need to be prominently disclosed.

20 NASAA strongly believes that sponsors cannot disclose away all duties and potential liability for unsound, unfair transactions. However, providing full disclosure on the nature of projections and allowing investors to consider data with significant warnings will be a net benefit to investor protection.

21 *See, e.g.,* Rachita Gullapalli, *Misconduct and Fraud in Unregistered Offerings: An Empirical Analysis of Select SEC Enforcement Actions*, SEC Division of Economic and Risk Analysis (Aug. 2020), https://www.sec.gov/files/Misconduct%20And%20Fraud%20In%20Unregistered%20Offerings.pdf (stating that many fraudulent exempt offerings use projections and forward looking statements to lure investors by promising high returns at low or no risk).

22 *See* Proposal, Section VI.A.

de-SPAC mergers. For those SPAC entities whose operating agreements allow for an extension of the 18-24 month time horizon, an extension to the safe harbor rule may be appropriate. Any provisions permitting extensions and the terms of such allowances would need to be closely scrutinized, and align with the final rules put forth by the Commission. Extended time horizons should also include the ability for shareholders to redeem without penalty.

## VI. Conclusion

NASAA is pleased to see that the Commission plans to set guidelines around SPACs to better align these offerings with other methods of bringing private entities to the public market. For the reasons discussed above, NASAA broadly supports the Proposal. However, we believe that there are areas for improvement as described above. Thank you for considering these views. NASAA looks forward to continuing to work with the Commission in the shared mission to protect investors. Should you have questions, please contact either the undersigned or NASAA's General Counsel, Vince Martinez, at (202) 737-0900.

Sincerely,

Melanie Senter Lubin
NASAA President
Maryland Securities Commissioner