american securities association
America's Voice for Main Street's Investors

May 27, 2022

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

Re: Special Purpose Acquisition Companies, Shell Companies, and Projections (Release Nos. 33-11045, 34-94546, IC-34549, File No. S7-13-22)

Dear Ms. Countryman:

The American Securities Association (ASA)[1] submits these comments in response to the Securities and Exchange Commission's (SEC) proposed rules regarding special purpose acquisition companies (SPACs) and related issues (Proposal). While the ASA generally welcomes efforts to enhance transparency and investor protections in the SPAC market, we are concerned the Proposal would impose unwarranted liabilities and disincentivize financial institutions from advising on SPAC or "de-SPAC" transactions. This could have the effect of further increasing risks to investors and diminishing due diligence associated with SPAC deals.

I. Introduction.

SPACs are an innovative way for private companies to access the public markets. SPACs allow a company to list on a national stock exchange with the intent of entering into a business combination with a target company within a certain timeframe (typically two years). Once the business combination is complete, the combined company continues to be publicly traded under the SPAC's listing and continues to operate the business of the target company.

The growth and interest in the SPAC market – driven in part by celebrity endorsements of certain deals and a spike in SPAC offerings in 2020 – has rightfully gained the attention of policymakers. The unique function of the SPAC raises several important investor protection questions and warrants a thorough examination by the SEC and Congress.

[1] The ASA is a trade association that represents the retail and institutional capital markets interests of regional financial services firms who provide Main Street businesses with access to capital and advise hardworking Americans how to create and preserve wealth. The ASA's mission is to promote trust and confidence among investors, facilitate capital formation, and support efficient and competitively balanced capital markets. This mission advances financial independence, stimulates job creation, and increases prosperity. The ASA has a geographically diverse membership of almost one hundred members that spans the Heartland, Southwest, Southeast, Atlantic, and Pacific Northwest regions of the United States.

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Last year, the ASA released a set of recommendations for how to improve the SPAC market.[2] These recommendations include:

- SPAC sponsors should be required to provide disclosure regarding their economic stake and potential outcomes from a future merger transaction;

- Certain enhanced disclosures may benefit investors in SPAC transactions. For example, SPACs should clearly disclose to investors that a deal may not come to fruition and that shares may only be redeemed at a certain price. Investors should also be provided with merger information and a proxy statement (or a summary document of the merger document), including information for how the valuation was determined;

- A Form S-4 and proxy statement should be filed at the same time (or shortly thereafter) a deal is announced; a SPAC should also have to publicly file a description of the transaction and how they determined valuation;

- SPAC sponsors should be subject to at least a one-year lockup in their shares from the date that the merger is completed; and

- Any sales within a certain period (e.g. three years) by a SPAC sponsor should be considered a "distribution" under SEC rules.

These recommendations were largely focused on disclosure and ensuring that any potential conflicts of interest do not harm investors during de-SPAC process. The Proposal, by contrast, seeks to impose traditional initial public offering (IPO) rules on de-SPAC transactions and would, in some instances, vastly, unnecessarily and inappropriately expand underwriter liability beyond what currently applies in the traditional IPO process.

The ASA wishes to provide the following recommendations and observations regarding the Proposal:

I. The SEC has not provided sufficient time for the public to submit feedback on the Proposal and has failed to consider the cumulative impact of outstanding rule proposals.

The Proposal is just one of the many complex and consequential rulemakings the SEC has proposed in recent months. To date this year the SEC has proposed sixteen new rulemakings, in addition to several others that were proposed at the end of 2021. Most of these proposals run to

[2] https://www.americansecurities.org/post/direct-listings-harm-investors-and-undermine-market-confidence

hundreds of pages in length, and often include hundreds of questions that commenters must consider when assessing the impact of potential new rules.

The Proposal itself is 372 pages and includes several specific questions, some of which hint at further mandates that are not fully explored or analyzed in the release. Yet the SEC provided the public only thirty (30) days to comment on the Proposal. This is an inadequate amount of time for the public to properly consider how the Proposal will affect the SPAC market and investors, particularly when many entities are simultaneously considering and developing comments on over a dozen other rulemakings from the SEC.

The ASA reiterates our call for the SEC to immediately extend the comment period for every outstanding rule proposal by a minimum of ninety (90) days. Doing so would allow the SEC to properly consider specific comments on each proposal and to assess the cumulative effect of its current regulatory agenda.[3]

II. The SEC should refrain from adopting proposed Rule 140a as it would disincentivize investment banks from advising on de-SPAC transactions.

Proposed Rule 140a would deem 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 engaged in the distribution of the securities of the surviving public entity….within the meaning of Section 2(a)(11) of the Securities Act."[4] Additionally, the Proposal would expand the definition of "underwriter" to potentially include lawyers, accountants, or other parties that may have been involved with the de-SPAC transaction.

As a threshold matter, we do not believe the SEC should equate, for regulatory purposes, a de-SPAC transaction with a registered offering of securities underwritten by a syndicate of investment banks. The issuance of securities of the combined company in a de-SPAC transaction to equity owners of the target company is not at all similar to the issuance of IPO securities by the Issuer in an IPO transaction. The investors in the securities issued in an IPO transaction typically make a new investment in a business with which such investors have no prior relationship. To the contrary, in a de-SPAC transaction, the securities issued to the equity owners of the target company just represent a continuing equity interest in the business of the target company in which they already own an investment interest. The relationship of such equity owners to the combined company, and the interests and risks faced by such equity owners in a de-SPAC transaction bear little resemblance to those of a typical investor in an IPO.

[3] https://www.americansecurities.org/post/asa-urges-sec-to-extend-comment-period-for-90-days
[4] Proposal at 96

Additionally, the relationship of the investors in the SPAC to the combined company, and the interests and risks faced by the SPAC investors in the de-SPAC transaction are quite dissimilar to those of a typical IPO investor. The SPAC investors have an opportunity to vote to approve or disapprove the de-SPAC transaction, and also have the right to redeem their stock back in the SPAC, regardless of whether they vote to approve the de-SPAC transaction, after the terms of the de-SPAC transaction have been disclosed. And, in many recent de-SPAC transactions, a majority of the SPAC shareholders have in fact elected to redeem, demonstrating the power of the protections currently made available to SPAC investors.

Further, the role of an investment bank that assists with a de-SPAC transaction is not an underwriting role. Typically, the investment banks provide M&A advisory services that do not involve any underwriting services or any services involving the distribution of any securities. These services are more akin to that the services provided by a firm acting as financial advisor to company that is entering into a stock-for-stock merger. In a stock-for-stock merger, an investment bank may run a sale process, assist with due diligence, assist the company with valuation, assist with negotiations, assist the company in crafting its rationale for the transaction, and assist the company in scheduling meetings with institutional investors to discuss the rationale for the merger. These are exactly the same type of functions that an investment bank performs with a de-SPAC transaction. Likewise, if an investment bank assists a SPAC with a PIPE to provide additional financing for the de-SPAC transaction, the PIPE is typically a private placement by the SPAC to QIB investors on terms negotiated by the QIB investors. No underwriting activity is involved in these transactions.

The Proposal would also expand liability for financial advisors in a de-SPAC transaction beyond what currently applies to underwriters in traditional IPOs. In a traditional IPO, Section 11 underwriter liability is typically limited to the amount of securities each underwriter purchased from an issuer, and the entire underwriting typically involve no more than 20% to 30% of the equity value of the issuer. Under the Proposal, except for the sponsor shares, 100% of the shares of a de-SPAC'd company (i.e. the shares being issued to the private company shareholders and shares that continue to be held by non-redeeming SPAC shareholders) would be subject to underwriter liability. Imposing underwriter liability with respect to these two categories of shareholders is fundamentally unfair: the continuing equity holders of the target company are simply continuing an investment in a business in which they previously invested, and the SPAC shareholders have voting and redemption rights to protect their interests. At the same time, the investment bankers are not underwriting any securities: any distribution of securities typically is being conducted directly by the SPAC and the other companies conducting the de-SPAC transaction, and not through the facilities of any investment banking firm.

Assuming the "price per share" is approximately $10.00 (which is the price typically used to determine value), if the amount being "distributed" is equivalent to the amount of shares being

registered on the S-4, then the Section 11 liability could be in the billions of dollars, which would significantly exceed the liability assumed by underwriters in the vast majority of IPOs.

Additionally, we believe this proposal is unlawful in that it is in direct contradiction of Section 11(e) of the Securities Act, which states that "in no event shall any underwriter (unless such underwriter shall have knowingly received from the issuer for acting as an underwriter some benefit, directly or indirectly, in which all other underwriters similarly situated did not share in proportion to their respective interests in the underwriting) be liable in any suit…for damages in excess of the total price at which the securities underwritten by him and distributed to the public were offered to the public."

In a traditional IPO, investment banks understand the amount of potential liability they are assuming for a transaction and can factor in that liability when deciding what fee to charge an issuer. It is unclear how Section 11(e) would apply to investment banks that are deemed "underwriters" in a de-SPAC transaction. If Section 11(e) doesn't apply, each investment bank involved a de-SPAC transaction (whether as a financial advisor, IPO underwriter, or capital markets advisor), could potentially have liability on the entire amount of the securities being distributed in the de-SPAC transaction. This risk would make it untenable for investment banks to continue advising on de-SPAC transactions, and as a result, the regulation could have the effect of shutting down the market.

In her dissenting statement, Commissioner Peirce also noted that the Proposal "describes at great length court cases and Commission guidance on the determination of underwriter status, it contains only a brief analysis of how those cases apply here."[5] The end result, according to Commissioner Peirce, would be that "SPAC underwriters will do everything possible to avoid being captured by the rule, such as demanding all compensation up front, a result that may not benefit SPAC investors." The ASA echoes these concerns and predictions.

The activities of investment banks involved in de-SPAC transactions are much more similar to the activities such firms conduct when acting as financial advisors in a stock-for-stock merger transaction.

Accordingly, for the reasons described above, we urge the SEC to refrain from adopting proposed Rule 140a.

III. <u>The elimination of the safe harbor for forward-looking statements under the Private Securities Litigation Reform Act (PSLRA) is unlawful</u>.

[5] https://www.sec.gov/news/statement/peirce-statement-spac-proposal-033022

The Proposal would – without any authorization by Congress – amend the definition of a "blank check" company under the PSLRA to prevent SPACs from utilizing the PSLRA safe harbor for forward-looking statements. This aspect of the Proposal is in direct opposition to the provisions of the Proposal that require the SPAC to disclose the material reasons for which the SPAC believes its proposed de-SPAC transaction is fair to its public shareholders. As a part of assessing whether a proposed de-SPAC transaction is fair to the public shareholders of the SPAC, most SPAC's would want to consider the future earnings capacity of the business of the target company. Disclosure of information about how a company evaluates or assesses the future earnings capacity, or the likely future earnings, of its business or of a business that it seeks to acquire is the exact type of information that the PSLRA was enacted to protect, in order to encourage the disclosure of this type of forward-looking information. This Proposal ignores the statutory intent of encouraging disclosure of forward-looking information by providing a disclosure framework for a safe harbor, and simply demands the disclosure of forward-looking information, while at the same time stripping away the carefully crafted statutory safe harbor protections.

The intent of removing the safe harbor for de-SPAC transactions is undeniable – it would open SPACs to a flood of private litigation that, when added to other provisions of the Proposal, would effectively kill the existing SPAC market. Worse, the SEC is seeking to amend the PSLRA on its own without any explicit statutory authority or other directive from Congress. This type of legislation-by-rulemaking is unlawful and outside the bounds of the Administrative Procedure Act (APA). The SEC should drop this idea and recognize that it has no legal authority under law to change Congressional statutes on its own.

IV. Certain rules that would result in negative treatment of companies that list on an exchange via a SPAC transaction should be eliminated.

Under current rules, a company that elects to go public via a SPAC would be subject to certain restrictions that do not exist for companies that have gone public via a traditional IPO. We believe that as the SEC seeks to modernize rules related to SPACs it should consider easing some of these restrictions, which include:

- Rule 144(i) which makes it difficult for investors to re-sell restricted securities of a de-SPAC'd company;
- Rule 139(a)(1)(ii), which makes broker-dealers unable to rely on the standard Rule 139 safe-harbor for research reports following a de-SPAC tranaction;
- Rule 405, which includes de-SPAC'd companies as "ineligible issuers", thereby prohibiting them from using free-writing prospectuses during a registered securities offering and from being a Well-Known Seasoned Issuer (WKSI); and

- Form S-8, which makes de-SPAC'd companies ineligible to file a Form S-8 for 60 days following a de-SPAC.

Additionally, as currently drafted the Proposal and its expanded liability for underwriters would significantly alter the regulatory framework with respect to existing SPACs that were formed and entered into contracts with investment bankers and others in reliance on the existing rules. This type of retroactive application of SEC rules to existing SPACs would be inherently unfair and harmful to SPACs, SPAC investors and investment bankers and other third parties that have entered into contracts with SPACs. To the extent the SEC ultimately decides any new rules for SPACs are warranted, those rules must only be applied prospectively to SPACs formed *after* the effective date of a final rule.

V. Conclusion.

The ASA welcomes the opportunity to work with the SEC and Congress on improvements to SPAC market. However, as discussed throughout this letter, we believe several key aspects of the Proposal are unlawful and must be reconsidered. Some firms will doubtless view the Proposal as regulatory overreach, resulting in litigation challenging some of the proposed new rules, should they be adopted. We look forward to working with commissioners and staff of the SEC on this and other issues critical to the American capital markets.

Sincerely,

Christopher A. Iacovella

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