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Don't Get Burned: Why the DE-SPAC Transaction Must Be Excluded From the PSLRA's Safe Harbor Provision For Forward-Looking Statements

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Comment

DON'T GET BURNED: WHY THE DE-SPAC TRANSACTION MUST BE EXCLUDED FROM THE PSLRA'S SAFE HARBOR PROVISION FOR FORWARD-LOOKING STATEMENTS

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I. STOKING THE FLAMES: AN INTRODUCTION

Sound the alarm, the markets are HOT![1] The initial public offering (IPO) market is having a major moment; companies are racing to bring their organizations public, and investors are quickly jumping on board.[2] In 2021, the market saw major household companies enter the public arena, including the likes of Airbnb, Robinhood, and DoorDash.[3] But this was just the ignition point; the IPO market saw a "record-breaking" 1,000 deals in 2021, the IPOs strongest year in history.[4] Within this IPO boom, Wall Street saw investors "flock" to special purpose acquisition companies (SPACs)—an alternative investment vehicle to the traditional IPO—which promise higher returns than traditional IPOs.[5] In 2021, SPACs made up

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1. *See* Eric J. Savitz, *Get Ready for a Crazy Wave of IPOs. Here Are the Ones to Watch*, BARRON'S (Aug. 31, 2020), https://www.barrons.com/articles/the-ipo-market-is-about-to-go-crazy-here-are-the-ipos-to-watch-51598658370 [https://perma.cc/6Q44-5UVY] (explaining that a "flurry" of companies are about to go public and offer their shares for the first time to the public markets).

2. *See id.* (detailing the "flurry" of IPOs entering the public markets following the March 2020 economic downturn).

3. *See id.* (highlighting major companies that went public in 2020); *see also* Margaret Giles, *The Biggest IPOs of 2021*, MORNINGSTAR (Dec. 15, 2021), https://www.morningstar.com/articles/1072332/the-biggest-ipos-of-2021 [https://perma.cc/8QKG-GTJC] (explaining that 2021 had a record number of companies go public, due in part to "well-funded startups drum[ming] up investor enthusiasm that led to massive public debuts").

4. *See* Emily Bary, *The Record-Breaking IPO Market in 2021 Masked Some Problems Under the Hood*, MARKETWATCH (Dec. 24, 2021, 7:44 AM), https://www.marketwatch.com/story/there-were-1-000-ipos-in-2021-for-the-first-time-but-there-may-be-some-problems-under-the-hood-11640115839 [https://perma.cc/4VHC-7D9X]. The market saw over 1,000 offerings listed by the end of December and a record $315 billion raised. *See id.*

5. *See* Alexander Osipovich & Dave Michaels, *Investors Flock to SPACs, Where Risks Lurk and Track Records Are Poor*, WALL ST. J. (Nov. 13, 2020, 5:28 PM), https://www.wsj.com/articles/investors-flock-to-spacs-where-risks-lurk-and-track-records-

more than half of all IPO debuts—out of 1,000 IPO offerings, 606 were SPACs.[6] This SPAC explosion has been dubbed "spectacular" and the "gateway to alternative investments" for unsophisticated investors, despite concerns that these investment vehicles skimp on investor protections usually found in traditional IPOs.[7]

So, what is a SPAC, and why are they so popular? First, a brief explanation of the traditional IPO transaction: to start, a private operating company—with commercial operations and assets—announces that it wants to go public.[8] The company then files a registration statement with the U.S. Securities and Exchange Commission (SEC).[9] The registration statement includes the company's prospectus; this document presents disclosures about the company's financial condition, the IPO terms, and other company insights.[10] The SEC staff then reviews the registration statement, including the prospectus, to ensure that it complies with federal securities law requirements.[11] The SEC maintains that the review is not a guarantee that a company's disclosures are complete or accurate, though the process often results in changes to the prospectus to comply with the applicable

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are-poor-11605263402 [https://perma.cc/7RGR-R49D] (explaining that individual investors turn to SPACs to invest in startups from "buzzy sectors," such as cannabis and electric vehicles, despite a lack of investor protections found in traditional IPOs).

6. *See* Bary, *supra* note 4 (noting that out of the 606 SPACs offered in 2021, 298 were offered in the first quarter of the year).

7. Camila Domonoske, *The Spectacular Rise of SPACs: The Backwards IPO That's Taking Over Wall Street*, NPR (Dec. 29, 2020, 5:00 AM), https://www.npr.org/2020/12/29/949257672/the-spectacular-rise-of-spacs-the-backwards-ipo-thats-taking-over-wall-street [https://perma.cc/4CWG-92AM]; *see also* Shuli Ren, *SPACs Are Hot Because They Are the 'Poor Man's Private Equity Funds'*, BLOOMBERG BUSINESSWEEK (March 2, 2021, 5:00 AM), https://www.bloomberg.com/news/articles/2021-03-02/why-spacs-are-so-popular-they-re-the-poor-man-s-private-equity-funds [https://perma.cc/D36Q-AP3V] (asserting that SPACs appeal to the masses because they allow unsophisticated investors to invest in "hot" companies before they go to the public market, which is normally reserved for wealthy individuals and companies); *see also* Osipovich & Michaels, *supra* note 5 (explaining that companies turn to SPACs because the investment vehicle is subject to less safeguards than the traditional IPO; specifically, SPACs allow companies to make growth and future earnings projections with significantly lower liability risks than traditional IPOs).

8. *See* SEC OFF. OF INV. EDUC. & ADVOC., INVESTOR BULLETIN: INVESTING IN AN IPO 1 (Feb. 25, 2013) [hereinafter INVESTOR BULLETIN], https://www.sec.gov/files/ipo-investorbulletin.pdf [https://perma.cc/F8RW-H22J] (defining "initial public offering" as the first time a private company offers shares of capital stock to the general public for purchase).

9. *See id.* (explaining that an offering is registered when a company files a registration statement with the SEC, normally a Form S-1, which includes the company's prospectus).

10. *See id.* (explaining that the prospectus document contains information about the company's financial condition, management, the IPO terms, as well as a description of the company and its business).

11. *See id.* (elucidating that the review process is focused on finding disclosures that violate SEC rules and applicable accounting standards, or that are materially deficient because they lack sufficient explanation of clarity).

disclosure requirements.[12] Once the company has addressed compliance concerns, the SEC will declare the registration statement effective, allowing the IPO to proceed.[13] The company then attempts to solicit investors using the prospectus, which investors rely on to determine whether the offering is a good investment.[14]

A SPAC flips the traditional IPO process around and provides a much faster option for companies to go public than a traditional IPO.[15] At its IPO, SPACs are shell companies—entities with no commercial operations.[16] Unlike companies participating in traditional IPOs, SPACs do not have to disclose historical financial results or non-cash assets in the IPO.[17] Consequently, the SPAC's registration statements mainly include "boilerplate" language and biographies from the sponsors—i.e., the SPAC managers and founders—in their registration statement.[18] This allows the

12. *See id.* (clarifying that the registration statement review process does not claim to certify the completeness or accuracy of the statements made within the documents, nor does the staff seek to evaluate the merits of the IPO or the appropriateness for investors). The onus is on the company to provide complete and accurate disclosures to investors. *See id.* (explaining that the company and those who assist it in preparing the registration documents are responsible for the information provided within).

13. *See id.* (explaining that the staff will not declare a registration statement effective if the staff believes the statement is incomplete or inaccurate in any respect).

14. *See id.* (providing that "it is important [for investors] to read the prospectus because it provides information regarding the terms of the securities being offered as well as disclosure regarding the company's business, financial condition, management and other matters that are key to deciding whether the offering is a good investment").

15. *See* Ramey Lane & Brenda Lenahan, *Special Purpose Acquisition Companies: An Introduction*, HARV. L. SCH. F. ON CORP. GOVERNANCE (July 6, 2018), https://corpgov.law.harvard.edu/2018/07/06/special-purpose-acquisition-companies-an-introduction/ [https://perma.cc/VP4U-LFNS] (explaining that SPAC financial statement and disclosures in the IPO registration statement are short compared to the traditional IPO, meaning they can be prepared and reviewed by the SEC in a much shorter time frame); *see also* Daniele D'Alvia & Milos Vulanovic, *A Rethinking of U.S. Forward Looking Statements in SPACs*, FORDHAM J. CORP. & FIN. L. BLOG (July 13, 2021), https://news.law.fordham.edu/jcfl/2021/07/13/a-rethinking-of-u-s-forward-looking-statements-in-spacs/ [https://perma.cc/9ZKN-GHRK] (positing that the SPAC transaction "reverses the normal IPO procedure," as it is composed of investors seeking an operating company instead of an operating company seeking investors, as in a traditional IPO).

16. *See* SEC Off. of Inv. Educ. & Advoc., *What You Need to Know About SPACs – Updated Investor Bulletin,* U.S. SEC (May 25, 2021), https://www.sec.gov/oiea/investor-alerts-and-bulletins/what-you-need-know-about-spacs-investor-bulletin [https://perma.cc/2D4Y-YHTM] [hereinafter *What You Need to Know About SPACs*] (explaining that a SPAC goes through an IPO as a company without any underlying operations or assets other than cash, whereas a traditional IPO entails an operating company with a business operations and diverse assets).

17. *See* Lane & Lenahan, *supra* note 15 (providing that the SEC review process typically takes eight weeks to complete because the registration statements are very short and staff comments are typically light).

18. *See id.*

SEC to conduct a quicker review of the SPAC's registration documents, but it also forces investors to rely on the SPAC sponsors to sell them on the merits of investing in the SPAC.[19]

Once the sponsors have identified a private operating company (the "target company") with which to merge, the SPAC sponsors and target company leadership will negotiate the necessary terms to complete a merger, referred to as the "business combination."[20] After the parties have agreed upon the terms of the business combination, the SPAC's sponsors make an official merger announcement to the public and the SPAC's shareholders.[21] Following the announcement, the SPAC is required to either hold a shareholder vote to approve the merger or provide a tender offer.[22] If the merger is approved by the shareholders, the SPAC and the target company will complete the merger resulting in a publicly-traded operating company.[23] This process is referred to as the "de-SPAC transaction."[24]

The de-SPAC transaction amalgamates several elements of a public offering with aspects not typically found in a traditional IPO, including required redemption offers for the SPAC's shareholders and a limited time frame to consummate a merger with a target company.[25] As in a traditional IPO, the de-SPAC transaction—rather than the SPAC IPO—

19. *See id.* (emphasizing the need for investors at the IPO stage to evaluate the background of a SPAC's sponsors before investing because the investment vehicle lacks an operating history, as compared to a traditional IPO).

20. *See id.* (providing that the initial business combination is normally structured as a reverse merger where the private operating company merges into the SPAC).

21. *See* Lane & Lenahan, *supra* note 15 (explaining that once terms have been agreed upon, the SPAC may seek additional financing through a private equity in public equity (PIPE) commitment, after which an announcement about the terms of the merger and the additional financing will be released).

22. *See id.* (explaining that at this stage, the shareholders are given the option to sell back their SPAC shares in exchange for their *pro rata* share).

23. *See id.* (establishing that the business combination cannot be completed unless the following requirements are met: the proposed terms are approved by shareholders; the financing conditions are satisfied; and the acquisition agreement terms are met).

24. *See id.* (defining "de-SPAC transaction" as the receipt of shareholder approval, the satisfaction of relevant conditions, and the consummation of the merger between the SPAC and target company resulting in a publicly traded operating company). Typically, the de-SPAC transaction requires a majority of SPAC shareholders to give approval. *See* Bruce A. Ericson, Ari M. Berman & Stephen B. Amdur, *The SPAC Explosion: Beware the Litigation and Enforcement Risk*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Jan. 14, 2021), https://corpgov.law.harvard.edu/2021/01/14/the-spac-explosion-beware-the-litigation-and-enforcement-risk/ [https://perma.cc/Z9VB-BY5D].

25. *See* Ramey Layne, Brenda Lenahan & Sarah Morgan, *Update on Special Purpose Acquisition Companies*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Aug. 17, 2021), https://corpgov.law.harvard.edu/2020/08/17/update-on-special-purpose-acquisition-companies/ [https://perma.cc/DUA7-N4V5] (noting that compared to the traditional IPO, the de-SPAC transaction allows special considerations for investors, including: "limited recourse to the SPAC's IPO proceeds if the transaction

brings a private operating company public; in other words, the public has the first opportunity to purchase the company's securities in the de-SPAC transaction.[26] The SEC allows SPACs to include forward-looking statements in their proxy statements during the de-SPAC transaction; however, traditional IPOs are barred from doing so.[27] These forward-looking statements are predictions about the future economic performance of a company, such as a company's expected future profits and other financial projections.[28] Due to the highly "speculative" nature of these statements, they are subject to extensive regulation by the Private Securities Litigation Reform Act (PSLRA) and other securities laws.[29]

Certain groups argue that, as it stands, forward-looking statements made during the de-SPAC transaction fall within the protections of the PSLRA's safe harbor provision for forward-looking statements, which provides liability protection for certain companies that make projections that turn out to be false.[30] According to proponents of this idea, the safe harbor's protections make SPAC sponsors "comfortable" with presenting financial projections in the prospectus documents where a traditional IPO would not.[31] However, recent comments by John Coates, the SEC's for-

does not close; the requirement for the SPAC to make redemption offers to its common shareholders; and the SPAC's outside date").

26. *See* John Coates, *SPACs, IPOs and Liability Risk under the Securities Laws*, U.S. SEC (Apr. 8, 2021), https://www.sec.gov/news/public-statement/spacs-ipos-liability-risk-under-securities-laws [https://perma.cc/FTS4-3H52] (explaining that a SPAC's IPO is not usually regarded as the transaction that brings a private operating company public, instead the investment community recognizes the de-SPAC transaction as the real IPO of the SPAC process).

27. *See* Ericson et al., *supra* note 24 (asserting that, unlike a traditional IPO, the de-SPAC transaction "presents the opportunity for an operating company to speak more directly to the market about its financial prospects"); *see also* D'Alvia & Vulanovic, *supra* note 15 (explaining that SPACs are permitted to provide forward-looking statements in proxy statements, while IPOs face significant financial repercussions for doing so and are only permitted to share historical financial and business data).

28. *See* Brendan Carroll, Christopher Kercher, Michael Liftik, Ellison Ward Merkel, Andrew Rossman, Robert Schwartz & R. Brian Timmons, *Regulators Create Headwinds for SPACs*, J.D. SUPRA (July 2, 2021), https://www.jdsupra.com/legalnews/regulators-create-headwinds-for-spacs-3435297/ [https://perma.cc/2Q4S-HKJ7] (providing that forward-looking statements are "any statements about the future [of a company,] including expectations for revenue . . . growth[,]" which are "particularly important for private businesses whose valuation lies mostly in projected growth").

29. Coates, *supra* note 26 (explaining that forward-looking statements offer both advantages and disadvantages which prompt close regulatory scrutiny and guidance as required by the PSLRA, the Securities Act of 1933 ("Securities Act"), and the Securities and Exchange Act of 1934 ("Exchange Act")).

30. *See* Ericson et al., *supra* note 24 (establishing that financial projections made in the proxy or registration statements of the de-SPAC transaction typically receive protection under the PSLRA's safe harbor provision for forward-looking statements, whereas a traditional IPO does not receive these protections).

31. *See* Coates, *supra* note 26 (exploring commentator's claims that SPACs offer an advantage over traditional IPOs because they fall within the PSLRA's safe harbor, thus exposing the SPAC to lesser securities law liabilities).

mer Acting Director for the Division of Corporation Finance, suggested that this view "raises significant investor protection questions."[32] Specifically, Coates pointed to the PSLRA's legislative history, which includes statements indicating that the protections were only meant for "seasoned issuers" with an "established track-record," not unproven entities like those that frequently participate in the de-SPAC transaction.[33]

Congress adopted the PSLRA to address an influx of "frivolous" securities fraud lawsuits in the twentieth century.[34] In response, many businesses turned away from the public markets, instead opting to participate in private transactions.[35] This shift had severe ripple effects throughout the economy.[36] With the passage of the PSLRA, Congress sought to deter

32. *See id.* (raising investor protection concerns posed by commentator's claims that the safe harbor applies to financial projections made in the de-SPAC transaction's prospectus). Coates posed the following questions and investor protection concerns raised by allowing sponsors to include forward looking statements in the de-SPAC transaction:

> Are current liability protections for investors voting on or buying shares at the time of a de-SPAC sufficient if some SPAC sponsors or advisors are touting SPACs with vague assurances of lessened liability for disclosures? Do current liability provisions give those involved – such as sponsors, private investors, and target managers – sufficient incentives to do appropriate due diligence on the target and its disclosures to public investors, especially since SPACs are designed not to include a conventional underwriter at the de-SPAC stage? Moreover, is it appropriate that the choice of how to go public may determine or be determined by liability rules?

Id.

33. *See id.* (citing Debate in Senate to Override President's Veto, 141 Cong. Rec. S190602 (daily ed. Dec. 21, 1995)) (reflecting statements from Senator Diane Feinstein saying, "The provisions [of the PSLRA] are only available to companies with an established track record" and "I understand the safe harbor does not apply to a new company, but only applies to seasoned issuers").

34. *See* Marilyn F. Johnson, Karen K. Nelson & A. C. Pritchard, *Do the Merits Matter More? The Impact of the Private Securities Litigation Reform Act*, 23 J. L. ECON. & ORG. 627, 627–28 (2007) (explaining that the potential for "enormous" damages encouraged plaintiff's lawyers to bring "frivolous" securities fraud class actions against companies, which were often not based on a sustainable claim). Plaintiff's attorneys would file suits based on generic complaints when a company's projections did not come to fruition. *See id.* (noting that Congress viewed these cases as a dangerous nuisance to economic growth). These suits were filed right after a company's stock price fell, with the hope of finding "a sustainable claim not alleged in the complaint" during discovery. *See id.* (citing H.R. REP. NO. 104-50(1), 104th Cong., 1st Sess. (1995); S. REP. NO. 104-98, 104th Cong., 1st Sess., reprinted in [1995] U.S.C.C.A.N. 679).

35. *See* Laurie Smilan & Nicki Locker, *Saying So Long to State Court Securities Litigation*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Feb. 11, 2019), https://corpgov.law.harvard.edu/2019/02/11/saying-so-long-to-state-court-securities-litigation/ [https://perma.cc/ET9W-CT4Z] (illustrating the widespread effect that companies' decisions to shift to private transactions over public investments had on the national economy and individual investors by drawing attention to Congress' urgency to pass new legislation to address the problem).

36. *See id.*

these lawsuits and restore confidence in the public markets.[37] The PSLRA established a heightened pleading standard for plaintiffs to bring a securities fraud suit, which required a showing of fraudulent intent at the time of the complaint.[38] Additionally, the PSLRA created a safe harbor for forward-looking statements made by companies in registration and proxy statements.[39] The safe harbor protects certain businesses from civil liability when a qualifying forward-looking statement does not come to fruition.[40] A qualifying statement may not be materially false or misleading and must contain adequate cautionary language.[41]

Despite its broad protections, the safe harbor is limited in its application.[42] As indicated by the PSLRA's legislative history, Congress meant the provision to apply to "seasoned issuers" with an "established track record" to ensure that forward-looking statements are supported by data and past performance of a particular company.[43] Unlike established public companies, traditional IPOs, blank check companies—not to be confused with

37. *See* Christopher J. Hardy, Comment, *The PSLRA's Heightened Pleading Standard: Does Severe Recklessness Constitute Scienter?*, 35 U.S.F. L. REV. 565, 565–67 (2001) (citing H.R. REP. NO. 104-369, at 32 and 31 (1995) (Conf. Rep.)).

38. *See id.* at 567 (establishing that the PSLRA requires plaintiffs to "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind"); *see also* 15 U.S.C. § 78u-4(b)(2) (Supp. IV 1998).

39. *See generally* 15 U.S.C. § 78u-5(c); *see also* D'Alvia & Vulanovic, *supra* note 15 (explaining that the PSLRA's safe harbor provision for forward-looking statements "modified the qualification[s] for forward-looking statements under Section 11 of the Securities Act of 1933 and Section 10(b) of the Securities Exchange Act of 1934").

40. *See* 15 U.S.C. § 78u-5(c)(1)(A)–(B). The relevant section of the safe harbor reads as follows:

> (c) (1) [In a private securities fraud suit brought under 10b-5, an issuer] shall not be liable with respect to any forward-looking statement, whether written or oral, *if and to the extent that* —
> (A) the forward-looking statement is —
> (i) identified as a forward-looking statement, and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement; or
> (ii) immaterial; or
> (B) the plaintiff fails to prove that the forward-looking statement . . . was made with actual knowledge by that person that the statement was false or misleading; . . . .

Id. (emphasis added).

41. *Id.*

42. *See* D'Alvia & Vulanovic, *supra* note 15 (establishing that the PSLRA's safe harbor provision only applies to certain types of companies, as it specifically excludes forward-looking statements made by or in connection with blank check companies, penny stock issuers, or IPOs).

43. *See* Coates, *supra* note 26, at n.16. Congress created the safe harbor to "encourage" established, publicly traded, reporting companies to include forward-looking financial projections and plans within their proxy and registration statements. *See id.*

SPACs,[44] and penny stock issuers lack the requisite "established track record" that Congress sought to protect.[45] Consequently, the safe harbor expressly excludes, or "carves out," forward-looking statements made by or in connection with penny stock issuers, blank check companies, or traditional IPOs.[46]

Recently, Coates queried whether the de-SPAC transaction should fall within the IPO carve-out of the PSLRA's safe harbor provision.[47] The IPO carve-out, unlike the blank check or penny stock issuer carve-outs, is not defined by the PSLRA.[48] However, the PSLRA's legislative history indicates that the safe harbor's protections were only meant for "seasoned issuers" with an "established track record," not companies offering securities to the public for the first time.[49] As in a traditional IPO, the "economic essence" of the de-SPAC transaction is to bring a private operating company public for the first time.[50] In other words, it is the first time the public has the opportunity to review a company's business and financial information to determine if the company is a sound investment.[51] This

44. Despite their colloquial name, most SPACs do not meet the statutory definition to qualify as a blank check company. *See id.* at n.15 (providing that the PSLRA adopts Rule 419 of the Securities Exchange Act of 1934's definition of blank check company, which limits companies that qualify as blank check companies to those that issue penny stocks; most SPACs do not offer penny stocks, and thus do not qualify as blank check companies for purposes of the safe harbor provision).

45. *See* INVESTOR BULLETIN, *supra* note 8, at 2 (noting that the typical company participating in a traditional IPO does not have a prior reporting history, so investors must rely on the information provided within the prospectus); *see* Fidelity Viewpoints, *Trading Penny Stocks*, FIDELITY (May 18, 2021), https://www.fidelity.com/viewpoints/active-investor/trading-penny-stocks [https://perma.cc/EGY3-SBHK] (explaining that penny stocks often lack "reliable, readily available information," as they are not required to share the same information as most companies listed on public exchanges).

46. *See* Private Securities Litigation Reform Act of 1995 §§ 77z–2(b)(1)(B)–(C), 2(b)(2)(D) (prohibiting safe harbor protections for forward-looking statements made in connection with blank check companies, penny stock issuers, and IPOs).

47. *See* Coates, *supra* note 26 (questioning the notion that SPACs, specifically the de-SPAC transaction, are subject to lesser securities law liability than the traditional IPO because the de-SPAC transaction is essentially the initial public offering of a private operating company).

48. *See id.* (explaining that the PSLRA refers to the SEC's rules defining "blank check company" and "penny stock issuer," whereas the Act fails to provide any definition for "initial public offering"). Coates also notes that, for the purposes of the PSLRA, there is no case law or SEC rule that provides a definition for the offerings that fall within this category. *See id.* For the relevant statutory definitions, see *infra* note 141 (providing the definitions for blank check company and penny stock issuer, as defined in the PSLRA).

49. *See* Coates, *supra* note 26.

50. *Id.* (explaining that the generally accepted definition of an "IPO" is when a company initially offers its securities to the public for purchase, and that the de-SPAC transaction is generally understood as the part of the SPAC transaction where a private company first offers its securities to the public for purchase).

51. *Id.*

raises two questions: does the de-SPAC transaction qualify as a "seasoned issuer" with an "established track record," thus meriting the safe harbor's protection?[52] Or, is the de-SPAC transaction too similar to the traditional IPO, and thus too unproven, requiring that it fall within the IPO carve-out?[53]

This Comment argues that despite the apparent differences in their approach, the traditional IPO and de-SPAC transaction share a common purpose and goal: bringing a private operating company's securities to the public market for the first time.[54] This goal requires that the safe harbor's IPO carve-out be interpreted to include the de-SPAC transaction.[55] This Comment does not take issue with the current exclusions from the safe harbor provision.[56] Instead, it argues that the de-SPAC transaction's material similarities to the traditional IPO transaction compel inclusion under the safe harbor's IPO carve-out.[57] Additionally, this Comment asserts that heightened regulatory oversight and potential liability under federal securities law would deter SPAC sponsors from making overzealous forward-looking statements.[58] Further, this Comment asserts that this heightened regulatory scrutiny will address investor protection issues posed by the de-SPAC transaction—such as investors' reliance on insufficient due diligence and untested statements made by SPAC sponsors.[59]

Part II explores the background and procedures of the SPAC process and the traditional IPO transaction. Additionally, Part II provides the legislative history and purpose of the PSLRA and an exploration of its exclusions. Part III provides a narrative analysis of regulators' responses to the investor protection concerns raised by forward-looking statements made during the de-SPAC transaction. Part IV provides an analysis of the arguments surrounding the inclusion of the de-SPAC transaction within the PSLRA's IPO carve-out. Further, Part IV looks at the similarities between traditional IPOs and de-SPAC transactions, pointing to specific areas where investors are especially vulnerable to overzealous forward-looking statements made by SPAC sponsors in the de-SPAC transaction. Finally, Part V offers a call to action for regulators to intervene and provide inves-

52. *See id.* (questioning whether the PSLRA provides de-SPAC transactions protections from certain liability risks not offered to traditional IPOs).

53. *See id.*

54. For further development of this argument, see *infra* notes 170–204 and accompanying text (compelling regulators to include de-SPAC transactions within the IPO carve-out of the PSLRA's safe harbor provision).

55. *See id.*

56. *See id.*

57. *See id.*

58. *See id.* (establishing that further regulatory oversight of the forward-looking statements made during the de-SPAC transaction would deter overzealous plan sponsors due to potential liability under federal securities laws).

59. *See* Coates, *supra* note 26 (advancing the idea that immediate action is needed to address the loophole created by the PSLRA to protect investors from misleading statements made in conjunction with the de-SPAC transaction).

tors the necessary protections from these problematic forward-looking statements.

II. A TINDERBOX: CREATING THE PERFECT CONDITIONS FOR INVESTOR PROTECTION VIOLATIONS

Recently, the investment community saw a flare-up in the number of SPACs entering the public market.[60] These investment vehicles are often touted as a faster alternative to the traditional IPO, but many are asking, is it really worth the potential risks to investors?[61] Proponents of less regulatory oversight for SPACs claim that these investment vehicles offer distinct advantages to the traditional IPO: limited exposure to liability under securities laws for both the SPAC and target company.[62] Specifically, proponents suggest that the PSLRA's safe harbor applies to the de-SPAC transactions, thus allowing SPAC sponsors the ability to make financial projections and predictions within proxy statements.[63] However, the re-

60. *See* Bary, *supra* note 4 (explaining that 2021 was the first year in history that IPO listings broke 1000, of which 606 were SPACs). A SPAC is an investment vehicle that has increasingly been used to raise investment capital through an IPO. *See What You Need to Know About SPACs*, *supra* note 16. However, unlike other corporations, a SPAC does not have any underlying commercial operating business, nor does it have assets other than cash and limited investments, which includes proceeds from the IPO. *See id.*

61. *See* John Lambert, *Why So Many Companies Are Choosing SPACs Over IPOs*, KPMG https://advisory.kpmg.us/articles/2021/why-choosing-spac-over-ipo.html [https://perma.cc/PR7M-4X37] (last visited May 10, 2022) (explaining that one of the main advantages of a SPAC compared to a traditional IPO is faster execution; a de-SPAC transaction typically takes between three and six months, where as an IPO takes between twelve and eighteen months); *see* Coates, *supra* note 26 (outlining potential risks posed to investors by the influx of SPACs to the market, including "risks from fees, conflicts, and sponsor compensation, from celebrity sponsorship and the potential for retail participation drawn by baseless hype, and the sheer amount of capital pouring into the SPACs"); *see also* Noah Buhayar, Tom Maloney & Zija Song, *Wall Street Is Churning Out SPACs at Investors' Peril*, BLOOMBERG (Nov. 16, 2021), https://www.bloomberg.com/graphics/2021-what-is-a-spac-wall-street-investor-risk/ [https://perma.cc/X7P8-J9P4] (supplying critic commentary that the pressure faced by SPAC sponsors to complete a de-SPAC transaction before the deadline to return money to the SPAC's investors means that "desperate" sponsors will partake in riskier mergers).

62. *See* Coates, *supra* note 26 (describing SPAC proponents' argument that SPACs are subject to lesser securities law liability than the traditional IPO, while positing that these claims are unfounded and dangerous to investors).

63. *See id.* at n.27 (citing Chris Bryant, *Why Chamath Palihapitiya Loves SPACs So Much*, BLOOMBERG OPINION (Jan. 28, 2021), https://www.bloomberg.com/opinion/articles/2021-01-28/why-chamath-palihapitiya-loves-spacs-so-much [https://perma.cc/59GH-2XVT] (citing Haystack, *Alignment Summit Chats: SPACS (w/ Chamath Palihapitiya)*, YOUTUBE (Dec.2, 2020), https://www.youtube.com/watch?v3Q5eJjGgw [https://perma.cc/Z4J3-QMXP] (statement of Chamath Palihapitiya) ("Because the SPAC is a merger of companies, you're all of a sudden allowed to talk about the future. When you do that you have a better chance of being more fully valued."))); *see also* Ericson et al., *supra* note 24 (asserting that SPACs differ from traditional IPOs because they are allowed to make forward-looking statements in connection with the de-SPAC transaction, as they fall within the

cent influx of SPACs has brought with it an increase in SPAC-related litigation and a renewed focus on SPAC-related risks,[64] causing many commentators and regulators to question whether the safe harbor actually applies to de-SPAC transactions.[65] Further compounding these concerns, Coates warned that registration statements provided during the de-SPAC transaction may soon be subject to heightened regulatory scrutiny.[66] Specifically, Coates drew attention to the potential investor protection issues posed by allowing SPAC sponsors to make forward-looking statements in these filings.[67]

A. *The Kindling: A Brief Explanation of the SPAC Process*

As defined by the SEC, at the time of the SPAC's inception it is a shell company—a company with no "underlying operations or assets other than cash and limited investments, including the proceeds from [its] IPO."[68] The most common SPAC transaction is one in which the SPAC identifies and acquires a private operating company whose securities it will then bring to the public market, resulting in a public company.[69] SPACs are

PSLRA's safe harbor provision); *see also* Kevin Manne, *Investors Lose Out When Investing in 'Blank-Check' SPACs*, UBNow (Jan. 24, 2022), https://www.buffalo.edu/ubnow/stories/2022/01/blank-check-spacs.html [https://perma.cc/NE6Y-H3VE] ("Due to litigation concerns, companies that go public via a traditional initial public offering (IPO) cannot provide forward-looking information to investors—but SPAC acquisitions fall under different regulations that allow them to make financial projections").

64. *See* Leo Cho, SPAC Related Filings on the Rise, Sec. Class Action Clearinghouse (2021), https://securities.stanford.edu/news-reports/20210607-SPAC-Related-Filings-on-the-Rise.pdf [https://perma.cc/5H8Y-RV5X] (noting that SPAC-related litigation accounted for nearly fourteen percent of all securities class action lawsuits filed between January 1 and May 31 of 2021, up from one to two percent of total filings in 2019 and 2020).

65. *See* Roger Barton & Michael Ward, *SPACs and Speculation: the Changing Legal Liability of Forward-Looking Statements*, Reuters (July 7, 2021, 12:40 PM), https://www.reuters.com/legal/legalindustry/spacs-speculation-changing-legal-liability-forward-looking-statements-2021-07-07 [https://perma.cc/7YR7-6A23] (explaining that despite investor and company interest in SPACs, the recent influx of SPACs to the public markets has brought with it an increase in regulatory and legislative scrutiny, specifically in regards to the investor protection concerns raised by forward-looking statements made during the de-SPAC transaction).

66. *See* Coates, *supra* note 26 (warning investors, SPAC sponsors, and SPAC participants of the potential dangers of overstating SPACs protection from liability under securities laws).

67. *See id.*

68. *See What You Need to Know About SPACs*, *supra* note 16.

69. *See id.* (noting that the most common SPAC transaction is one where the SPAC acquires a private operating company and conducts a reverse merger where the private company merges into the SPAC, resulting in a publicly-traded company carrying out the target company's business); *see also* Tom Huddleston Jr., *What Is a SPAC? Explaining one of Wall Street's Hottest Trends*, CNBC (Feb. 23, 2021, 11:13 PM), https://www.cnbc.com/2021/01/30/what-is-a-spac.html [https://perma.cc/G8JF-MQ8E] (explaining that SPACs have no "explicit business plan other than to acquire or merge with an unspecified private company at some point"—the typical

usually created by a team of experienced institutional investors or individuals—and recently, an increasing number of celebrities—who provide the initial working capital in exchange for founder's shares.[70] In its IPO, the SPAC offers shares for cash.[71] Proceeds from this offering are then placed into a trust account for future use in its acquisition of a private operating company.[72] At the time of the IPO, neither the SPAC's sponsors nor investors know what the eventual target company will be.[73] Though, the SPAC's prospectus may identify a particular industry that the sponsors plan to target.[74] Consequently, investors rely on the SPAC sponsors' expertise and background to locate and acquire a target company within the period provided by the SPAC's governing instrument—typically eighteen to twenty-four months after the SPAC's IPO.[75] Once the SPAC's sponsors

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timeframe is two years after the SPAC's IPO); *see also Special Purpose Acquisition Company (SPAC)*, CORP. FINANCE INST., https://corporatefinanceinstitute.com/resources/knowledge/strategy/special-purpose-acquisition-company-spac/ [https://perma.cc/35TK-D5JV] (last visited Feb. 18, 2022) (providing that the SPAC structure—it is a shell company at the time of its IPO—allows investors to invest in a fund that will then be used to acquire one or more target businesses, which will be identified after the IPO); *see also SPACs Explained*, FIDELITY (Mar. 3, 2022), https://www.fidelity.com/learning-center/trading-investing/SPACs [https://perma.cc/D9QW-2P24] [hereinafter *SPACs Explained*] (explaining that after a SPAC identifies a target corporation, the SPAC will merge with or acquire the private operating company and continue its previous operations as a public company).

70. *See* Layne et al., *supra* note 25 (establishing that SPAC sponsors cover the expenses associated with the SPAC's IPO and a "modest" amount of working capital to fund operations through this transaction; in exchange, the sponsors will receive founders shares, which typically equal twenty-five percent of the number of shares registered for the IPO); *see* Amrith Ramkumar, *The Celebrities From Serena Williams to A-Rod Fueling the SPAC Boom*, WALL ST. J. (Mar. 17, 2021, 5:32 AM), https://www.wsj.com/articles/the-celebrities-from-serena-williams-to-a-rod-fueling-the-spac-boom-11615973578 [https://perma.cc/W47K-XFHX] (dubbing SPACs "cool" and noting that part of SPAC's recent popularity can be attributed to a wide variety of celebrity involvement). In addition to the founder's shares received, SPAC sponsors typically receive three to five percent of proceeds from the IPO and roughly five percent of the value from a merger. *See SPACs Explained*, *supra* note 69 (citing CFA Society Chicago Education Advisory Group, as of December 15, 2020).

71. *See What You Need to Know About SPACs*, *supra* note 16 (explaining that the SPAC invests the proceeds from its IPO, minus operating expenses, into a trust which is held by a third party until a de-SPAC transaction is successfully completed.); *SPACs Explained*, *supra* note 69 (establishing that the SPAC must place at least eighty-five percent of the IPO's proceeds into a trust account, and that they are usually invested in government bonds). Unlike the traditional IPO, SPACs cannot base stock value on previous financial performance—SPACs do not have any existing operations or business prior to the IPO. *See What You Need to Know About SPACs*, *supra* note 16. Thus, SPACs typically sell their shares for a "nominal" ten dollars per share. *Id.*

72. *See What You Need to Know About SPACs*, *supra* note 16.

73. *See id.* (explaining that SPAC sponsors and investors purchase shares in the SPAC's IPO without knowing what the target company will be).

74. *See id.*

75. *See id.* (explaining that the typical governing instrument of a SPAC requires the sponsors to complete a de-SPAC transaction within eighteen to twenty-four months of the IPO but noting that if the SPAC offers securities on an ex-

have identified a target company and negotiated the terms of the merger—the "business combination"—the two entities will engage in a de-SPAC transaction, resulting in a public operating company.[76] However, if the SPAC fails to consummate a business combination, the sponsors are required to liquidate the SPAC and return each investor's *pro rata* share.[77]

1. *The De-SPAC Transaction*

Once the two entities agree upon the terms of the business combination, they will make a formal announcement about the signing of the business combination agreement.[78] After this, sponsors are required to present shareholders with the opportunity to redeem their shares, and usually, the opportunity to vote about the proposed business combination.[79] At this point, the SPAC must provide shareholders with a proxy

change, it must complete the transaction within three years). If permitted by the governing document, sponsors may seek an extension, though it may require shareholder approval. *Id.*

76. *See* Lane & Lenahan, *supra* note 15 (explaining that once the SPAC has received the requisite shareholder approval, met the financing conditions, and consummated the merger, the resulting company will carry on the target company's operations as a public entity). SPACs often seek an additional round of financing prior to the signing of the business combination agreement, usually in the form of a private investment in public entity (PIPE) agreement to finance part of the purchase price. *See id.* (noting that after the PIPE investment is received, the SPAC's sponsors will make a formal announcement about the business combination agreement).

77. *See What You Need to Know About SPACs*, *supra* note 16 (explaining that sponsors' failure to complete a merger within the specified time frame will result in the SPAC's liquidation, at which time the shareholders will be entitled to their "their *pro rata* share of the aggregate amount then on deposit in the trust account").

78. For further details regarding the public announcement, see *supra* note 21 and accompanying text.

79. *See What You Need to Know About SPACs*, *supra* note 16 (noting that the SPAC's shareholders have the option to maintain their SPAC shares—which will be converted to shares in the company post-merger—or redeem their shares the *pro rata* amount of the funds held within the SPAC's trust account). According to stock exchange rules, not all SPACs are required to obtain shareholder approval to complete a de-SPAC transaction. *See* Lane & Lenahan, *supra* note 15 (noting that the necessity of holding a shareholder vote is determined by the structure of the de-SPAC transaction, but in most cases, a public vote of shareholders is required). Additionally, a shareholder vote does not have to be held if the sponsors or other affiliated entities hold enough votes to approve the transaction. *See What You Need to Know About SPACs*, *supra* note 16 (detailing the conditions that prompt a shareholder vote during the de-SPAC transaction). However, if a vote is required, shareholders vote via proxy to approve or disapprove the proposed business combination. *See SPACs Explained*, *supra* note 69 (explaining the shareholder voting process and requirements). "If more than 50% of shareholders approve and less than 20% vote for liquidation, then the transaction is approved and the acquired company is listed on an exchange [as a public company]." *See id.* However, "if more than 50% approve but more than 20% want to liquidate their shares, the escrow account is closed and funds are returned to public shareholders via a *pro rata* distribution of the net offering proceeds (less any fees for early redemption)." *See id.* At the time of the shareholder vote, most SPACs only need 37.5% of the

statement that outlines the terms of the business combination, the sponsors' interests, and the target company's business and operations.[80] Investors rely on this information to determine if they will exchange their SPAC shares for shares in the newly combined entity or if they will sell back their shares, thus withdrawing their support from the investment vehicle.[81] If the proposed business combination is approved, the two entities merge, and the newly combined company will carry on the original target company's business as a publicly-traded company.[82] As illustrated, SPACs offer private companies an alternative pathway to the status of a publicly-listed company.[83]

2. *SPAC Sponsors' Interests*

From the outset, SPAC sponsors have a significant financial incentive to complete a de-SPAC transaction.[84] Before the SPAC's IPO, all operating expenses are covered by the sponsors in the form of nonrefundable payments.[85] If the sponsors fail to identify and acquire a target company, the sponsors lose their investment.[86] Once the sponsors have successfully listed the SPAC for its IPO, the sponsors are permitted to purchase up to twenty percent of the SPAC's shares at a significant discount.[87] If the

public shares to vote in favor of the transaction, as 20% of the required "yes" votes are the founder's shares. *See* Lane & Lenahan, *supra* note 15 (noting that at the time of the SPAC's IPO, most SPAC sponsors agree to vote their founder's shares in favor of the business combination, which usually account for 20% of the SPAC's outstanding shares).

80. *See What You Need to Know About SPACs*, *supra* note 16 (noting that the proxy statement provides information about the business combination, including the target company's financial statements, the interests of parties involved with the transaction, and the capital structure of the combined entity following the business combination).

81. *See id.* (explaining that shareholders who decide to redeem their SPAC shares instead of converting them, will receive the *pro rata* share of the aggregate amount then on deposit in the SPAC's trust account).

82. *See id.*

83. *See id.* (noting the rise in popularity of SPACs as an alternative investment vehicle compared to traditional IPOs in bringing private companies to the public markets).

84. *See* Huddleston, *supra* note 69; *see also SPACs Explained*, *supra* note 69 (explaining that SPAC managers typically receive roughly five percent of a potential deal and a twenty percent stake in the merged company). In addition to the amount received for the completion of a business combination, a SPAC's sponsors typically hold twenty percent equity in the SPAC and receive three to five percent of the proceeds from the SPAC's IPO. *Id.*

85. *See* Max H. Bazerman & Paresh Patel, *SPACs: What You Need to Know*, HARV. BUS. REV. (July 2021), https://hbr.org/2021/07/spacs-what-you-need-to-know [https://perma.cc/UG8A-9WBY] (noting that sponsors invest risk capital to pay the requisite bankers, lawyers, and accountants to get the SPAC to the IPO stage, where the SPAC will receive additional capital).

86. *See id.*

87. *See* Amrith Ramkumar, *SPAC Insiders Can Make Millions Even When the Company They Take Public Struggles*, WALL ST. J. (Apr. 25, 2021, 4:51 PM), https://www.wsj.com/articles/spac-insiders-can-make-millions-even-when-the-company-

sponsors complete a de-SPAC transaction, these shares will be exchanged for shares in the newly combined company following the merger.[88] Once a target is identified, and the terms of the business combination have been agreed upon, the SPAC sponsors often enter into loan or securities agreements that finance part of the purchase price.[89] These agreements often involve loans from the SPAC sponsors, who receive shares or cash in exchange for their capital.[90]

In addition to sponsors' financial incentives, SPACs have seen an increasing number of celebrities participate in SPAC management.[91] During the recent deluge of SPACs, many sponsors turned to celebrities to draw in investors and set themselves apart from the competition.[92] Celebrities have made SPACs seem more accessible to the average retail investor, which has changed the perception of the investment vehicle, ultimately expanding SPACs' investor pool.[93] In exchange for the use of their celebrity status, sponsors offer celebrities the chance to serve as financial backers and board members for the SPAC.[94] Typically these celebrities do not make financial decisions as SPAC sponsors. Instead, they

they-take-public-struggles-11619343000 [https://perma.cc/SKW8-8RSS] (explaining that the "deep" discount SPAC sponsors receive allows them to make a profit even if the newly combined company struggles after the merger, when most investors lose money).

88. *See id.*

89. *See* Lane & Lenahan, *supra* note 15 (noting that SPACs often participate in a PIPE commitment in order to meet the financing conditions of the business combination agreement).

90. *See id.* (explaining that investors' rights and ownership interests in the merged company may be altered by SPAC sponsors entering into a securities or loan agreement, such as a PIPE investment, to raise funds for the de-SPAC transaction).

91. *See* Ramkumar, *supra* note 70 (asserting that celebrities from multiple backgrounds are a driving factor in the recent rise in SPAC offerings).

92. *See* Bailey Lipschultz, *Celebrity SPACs Leave Famous Winners Looking More Like Losers*, BLOOMBERG (Dec. 16, 2021 8:53 AM), https://www.bloomberg.com/news/articles/2021-12-16/celebrity-spacs-leave-famous-winners-looking-more-like-losers [https://perma.cc/PS37-7FYJ] (noting that a number of SPACs brought on celebrities as board members and financial backers, despite their lack of corporate expertise); *see also* SEC Off. of Inv. Educ. and Advo., *Celebrity Involvement with SPACs—Investor Alert*, SEC (Mar. 10, 2021), https://www.sec.gov/oiea/investor-alerts-and-bulletins/celebrity-involvement-spacs-investor-alert [hereinafter *Celebrity Involvement with SPACs—Investor Alert*] (explaining that celebrities, like other investors, can be "lured" into risky investments).

93. *See* Osipovich & Michaels, *supra* note 5 (explaining that celebrities have changed the perception of SPACs from sketchy investment vehicle that only brought "shaky" companies public to a more stable investment opportunity); *see also* Alexander Osipovich, *Blank-Check Boom Gets Boost From Coronavirus,* WALL ST. J. (July 13, 2020, 4:49 PM), https://www.wsj.com/articles/blank-check-boom-gets-boost-from-coronavirus-11594632601 [https://perma.cc/6R5L-WFD7] (noting that individual investors are becoming more interested in the "once obscure" investment vehicle due to participation by well-known business leaders and investors).

94. *See* Lipschultz, *supra* note 92 (providing examples of the incentives offered to celebrities in exchange for their promotion of the SPAC).

act as "promoters" for the SPAC.[95] These celebrities, like the other sponsors, have significant incentive to complete a de-SPAC transaction, as their reputation and financial investment are at risk.[96]

B. *The Tinder: A Brief Explanation of the Traditional IPO Transaction*

The term "IPO" typically refers to the "first time a company offers its shares of common stock to the general public for purchase."[97] As in the de-SPAC transaction, traditional IPOs are used by private operating companies to convert from private to public ownership via publicly-traded shares.[98] Unlike the de-SPAC transaction, the traditional IPO brings a private company—which has established operations and prior business history—to the public markets.[99] The private operating company participates in a traditional IPO once it has determined that it has adequate resources and capital to support the process' burdensome reporting and financial requirements.[100] After the company decides to pursue a traditional IPO, it is required to register the transaction with the SEC before it can offer its shares for purchase.[101] To register, the SEC requires the registering company to file a Form S-1 registration statement, which includes the prospectus.[102] The prospectus provides investors with infor-

95. *See* Steven Kurutz, *OK, What's a SPAC?*, N.Y. TIMES (July 13, 2021), https://www.nytimes.com/2021/02/27/style/SPACS-celebrity-craze.html [https://perma.cc/JBX5-PEVY] (explaining that celebrities act as strategic advisors in exchange for a stake in the SPAC).

96. *See id.* (noting that SPACs monetize a celebrity's reputation to bring in investors based on the investor's name recognition of that celebrity and, in exchange, the celebrity has the potential to earn a substantial return if the SPAC successfully merges with a target company).

97. INVESTOR BULLETIN, *supra* note 8, at 1 (providing the widely accepted definition for "traditional IPO").

98. *See Investing in IPOs and Other Equity New Issue Offerings*, FIDELITY, https://www.fidelity.com/learning-center/trading-investing/trading/investing-in-ipos [https://perma.cc/P6RD-MP4M] (last visited Apr. 11, 2022) (explaining that a traditional IPO is the first time a private company sells its stock to the public, making it a publicly owned entity).

99. *See What You Need to Know About SPACs*, *supra* note 16 (explaining that in a traditional IPO, the company going public has operations and assets other than cash).

100. *See id.* (noting that companies participate in traditional IPOs once they have established the necessary "resources and structures" to facilitate the shift to a public company).

101. *See* INVESTOR BULLETIN, *supra* note 8, at 1 (establishing that federal securities laws require companies to register the IPO transaction with the SEC prior to offering or selling their shares, unless the transaction is subject to an exemption).

102. *See id.* (outlining registration requirements for companies attempting to register an IPO transaction). Form S-1 provides investors with key business and financial information, so that they can make an informed investment decision about the company. *See Form S-1*, CORP. FINANCE INST., https://corporatefinanceinstitute.com/resources/data/public-filings/form-s-1/ [https://perma.cc/32Y6-NSLA] (last visited Apr. 11, 2022) (providing an explanation and example of the form's requirements).

mation about the company's business, including its management team, financial performance, and other relevant information that investors rely on to determine whether the offering is a good investment.[103] Once the SEC has reviewed and declared the registration statement effective, the company is allowed to proceed with the IPO.[104]

When a company decides to go public through a traditional IPO, it agrees to put itself through an expensive and time-consuming process where it is subject to both public and regulatory scrutiny.[105] Despite this challenging process, companies participate in IPOs for several reasons, including raising capital for the company, raising the company's public profile, and allowing the company's early investors to cash out all or some of their private shares in the IPO.[106] IPOs can be very beneficial to the participating company.[107] However, these benefits come with significant trade-offs, including significant oversight by regulators and stockholders.[108]

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103. *See* INVESTOR BULLETIN, *supra* note 8, at 1 (detailing the required disclosures found within a prospectus).

104. *See id.* (detailing the IPO registration process). The SEC's staff are tasked with monitoring IPO registration statements for compliance with federal securities laws. *See id.* Their review focuses on the statement's compliance with SEC rules and on disclosures that appear to be materially deficient in their explanation or clarity. *See id.* Following the SEC's initial review, the statement may be amended by the company. *See id.* The SEC maintains that despite its review, it is not guaranteed that the company's disclosure is complete or accurate, nor does it evaluate or draw conclusions about the merit of the investment. *See id.* Once the company has amended the registration statement to comply with the SEC's comments, the SEC will declare the registration statement effective. *See id.* However, the SEC's staff will not do this if they believe that the disclosures within the statement are incomplete or materially inaccurate. *See id.*

105. *See* Kate Ashford & John Schmidt, *What is An IPO?*, FORBES (Mar. 24, 2022, 5:56 PM), https://www.forbes.com/advisor/investing/initial-public-offering-what-is-an-ipo/ [https://perma.cc/EBM2-2DM6] (noting that a company participating in an IPO is required to file forms and financial disclosures with the SEC, as well as hire a private underwriter, and prepare itself for increased public scrutiny as it prepares for its IPO); s*ee* INVESTOR BULLETIN, *supra* note 8 (providing that among other disclosures, the company is required to file a Form S-1, which includes the prospectus and other disclosures about the company). Companies typically hire an underwriter, such as an investment bank, to assist management in preparing documents and organizing investment banking firms, which will share prior to the IPO in exchange for additional funding. *See* Ashford & Schmidt, *supra.*

106. *See* Ashford & Schmidt, *supra* note 105 (listing factors that may contribute to a company's decision to go public); *see also Investing in IPOs and Other Equity New Issue Offerings*, *supra* note 99 (providing a brief explanation of why companies choose to go public).

107. *See Investing in IPOs and Other Equity New Issue Offerings*, *supra* note 99 (noting that following a company's IPO, it is required to adhere to stringent reporting rules and requirements, while it is also beholden to its stockholders).

108. *See id.*

C. *The Flint: The Private Securities Litigation Reform Act and Its Exceptions*

A key distinction between a traditional IPO and the de-SPAC transaction is the participating company's ability to include forward-looking statements in its registration or proxy statements.[109] The SEC does not permit a company going public to make forward-looking statements in traditional IPOs.[110] Instead, Companies going through a traditional IPO are required to rely on prior earnings and financial statements to lure in investors.[111] SPAC proponents claim that the investment vehicle is not subject to the same securities law liabilities as a traditional IPO, which allows sponsors to include forward-looking statements in the de-SPAC transaction's proxy statements.[112] Those who indulge in this reasoning point to the PSLRA's safe harbor for forward-looking statements.[113]

1. *Forward-Looking Statements*

The use of forward-looking statements in proxy statements has long been a controversial subject amongst regulators, investors, and commentators.[114] So what are they? Forward-looking statements are statutorily defined in the U.S. Code.[115] It is a broad category that includes any

109. *See* D'Alvia & Vulanovic, *supra* note 15 (explaining that despite the obvious procedural differences between a traditional IPO and the de-SPAC transaction, the defining characteristic in each transaction is a company's ability to include forward-looking statements, rather than historical financial results, in its proxy statements.)

110. *See id.* Forward-looking statements are any statements about the future of a company, including expectations for revenue growth, which are particularly important for private businesses whose valuation lies mostly in projected growth. *See* Carroll et al., *supra* note 28.

111. *See* D'Alvia & Vulanovic, *supra* note 15.

112. *See id.* (providing arguments made by SPAC proponents in favor of including forward-looking statements in proxy statements made during the de-SPAC transaction); *see also* Coates, *supra* note 26 (outlining the arguments made by SPAC proponents that SPACs are subject to the PSLRA safe harbor for forward-looking statements).

113. *See* Coates, *supra* note 26 (noting that many point to the safe harbor to support the argument that SPACs are allowed to include forward-looking projections in their proxy statements without being subject to liability if they do not come to fruition).

114. *See id.* (highlighting multiple arguments pertaining to the potential investor protection issues raised by forward-looking statements); *see, e.g.*, Barton & Ward, *supra* note 65 (outlining the scrutiny forward-looking statements are receiving by regulators, Congress, and commentators because of their "perceived" impact on investor protections).

115. 15 U.S.C. § 78u-5(i)(1) (2012). The statutory provision provides:

The term "forward-looking statement" means—

(A) a statement containing a projection of revenues, income (including income loss), earnings (including earnings loss) per share, capital expenditures, dividends, capital structure, or other financial items;

(B) a statement of the plans and objectives of management for future operations, including plans or objectives relating to the products or services of the issuer;

statement made by a company about its financial projections, including revenue or income; operational projections, including management objectives for future operations or products; and future economic performance, including any discussion and analysis of financial conditions by management.[116] These statements are a double-edged sword—they contain informative predictions such as financial projections, but these predictions can prove to be speculative or misleading.[117] Consequently, forward-looking statements are highly regulated and subject to the provisions of the PSLRA.[118]

2. *The Legislative History and Purpose of the Private Securities Litigation Reform Act*

Throughout the twentieth century, the securities litigation system was overwhelmed with an influx of frivolous fraud lawsuits alleging violations of the federal securities laws in the hope that the defendant companies would quickly settle to avoid the expense of litigation.[119] To avoid the frustrations caused by these suits, companies began to favor private mergers and investments over going public.[120] The economy and small investors felt the detrimental effects of this trend.[121] In 1995, Congress decided to intervene with the passage of the PSLRA.[122] The PSLRA established

> (C) a statement of future economic performance, including any such statement contained in a discussion and analysis of financial condition by the management or in the results of operations included pursuant to the rules and regulations of the Commission;
> (D) any statement of the assumptions underlying or relating to any statement described in subparagraph (A), (B), or (C);
> (E) any report issued by an outside reviewer retained by an issuer, to the extent that the report assesses a forward-looking statement made by the issuer; or
> (F) a statement containing a projection or estimate of such other items as may be specified by rule or regulation of the Commission.

Id.

116. *Id.*

117. *See* Coates, *supra* note 26 (comparing the advantages and disadvantages of forward-looking statements in proxy statements).

118. *See id.* (explaining that forward-looking statements are highly regulated because of their highly speculative nature).

119. *See* Patrick Hall, *The Plight of the Private Securities Litigation Reform Act in the Post-Enron Era: The Ninth Circuit's Interpretation of Materiality in Employer-Teamster v. America West*, 2004 BYU L. REV. 863, 872–74 (establishing that the twentieth century was rife with frivolous "strike" class action lawsuits, which were brought by plaintiff's lawyers with the hope that the company would settle to avoid costly discovery and litigation expenses).

120. *See* Smilan & Locker, *supra* note 35 (establishing the business environment that prompted the passage of the PSLRA).

121. *See id.* (explaining that companies' hesitancy to participate in the public market spurred negative effects across the national economy).

122. *See* 140 CONG. REC. S3695, S3706 (1994) (statements of Sen. Dodd & Sen. Domenici); *see also* H.R. REP. NO. 104-369, at 31 (1995) (Conf. Rep.), *as reprinted* in 1995 U.S.C.C.A.N. 730, 730. Congress identified a number of those abuses in the PSLRA's conference report, stating:

sweeping revisions to the Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934 ("Exchange Act").[123] The PSLRA sought to prevent the abusive litigation that plagued federal courts by raising the evidence threshold for plaintiffs who sought to file a securities fraud claim against a company based on a forward-looking statement that failed to come to fruition.[124] Additionally, Congress modified the requirements

> The House and Senate Committees heard evidence that abusive practices committed in private securities litigation include: (1) the routine filing of lawsuits against issuers of securities and others whenever there is a significant change in an issuer's stock price, without regard to any underlying culpability of the issuer, and with only faint hope that the discovery process might lead eventually to some plausible cause of action; (2) the targeting of deep pocket defendants, including accountants, underwriters, and individuals who may be covered by insurance, without regard to their actual culpability; (3) the abuse of the discovery process to impose costs so burdensome that it is often economical for the victimized party to settle; and (4) the manipulation by class action lawyers of the clients whom they purportedly represent.

Id. Additionally, Congress observed that meritless securities fraud litigation "unnecessarily increase[d] the cost of raising capital and chill[ed] corporate disclosure, [and was] often based on nothing more than a company's announcement of bad news, not evidence of fraud." S. REP. NO. 104–98, at 4 (1995) (Conf. Rep.), *as reprinted* in 1995 U.S.C.C.A.N. 679, 683; *see* Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (1995) (codified as amended in scattered sections of 15 U.S.C. (2006)). As noted by R. Bruce Josten, former Executive Vice President of Government Affairs for the U.S. Chamber of Commerce,

> Those [congressional] hearings and studies demonstrated that a small coterie of plaintiffs' lawyers brought suit whenever a company's stock price fell for any reason, alleging that securities fraud was responsible. To serve as their ostensible clients, the lawyers recruited professional plaintiffs who bought a few shares of many companies' stock for the sole purpose of bringing a class action suit the day after the share price declined. The lawyers would file literally the same boilerplate complaint in case after case–sometimes even forgetting to change the names of the companies listed as the defendant. The point of this exercise was to extract hefty attorneys' fees from companies that couldn't afford years of litigation over nuisance suits.

Hall, *supra* note 119, at 873 n.52 (citing R. Bruce Josten, Executive Vice President of Government Affairs, United States Chamber of Commerce, *Letter to the U.S. Senate: PSLRA and the Uniform Standards Act* (Feb. 27, 2002)).

123. Securities Act of 1933, ch. 38, 48 Stat. 74 (codified as amended at 15 U.S.C. §§ 77a-b (1994)) (mandating that corporations disclose extensive information about themselves at the time they initially sell their securities); Securities Exchange Act of 1934, ch. 404, 48 Stat. 881 (codified as amended at 15 U.S.C. § 78a-7811 (1994)) (mandating that corporations with outstanding stock disclose material information on an ongoing basis after the initial offering of their securities).

124. *See* 15 U.S.C. § 78u(b)(4) (explaining that plaintiffs are now required to bring forward fraudulent statements made by the defendant, to allege that the fraudulent statements were reckless or intentional, and prove that they had suffered a *financial loss* as a *result of* the alleged fraud); *see also* Walter C. Somol, *Dredging the Safe Harbor for Forward Looking Statements–An Analysis of the Private Securities Litigation Reform Act's Safe Harbor for Forward Looking Statements,* 32 SUFFOLK U. L. REV. 265, 275–76 (1998) (noting that the PSLRA and the safe-harbor provision help "curb abusive private securities litigation," but also promote the "dissemination of forward-looking information").

for forward-looking statements in proxy statements by adding the PSLRA's safe harbor for forward-looking statements.[125]

3. *The Safe Harbor Provision for Forward-Looking Statements*

The PSLRA's safe harbor codifies the common law "bespeaks caution" doctrine.[126] This doctrine protects securities issuers[127] from claims of fraud based on a company's forward-looking statements, as long as that statement contains adequate cautionary language about the risks that could affect the statements.[128] Congress added this provision to create a more efficient market by encouraging companies to disclose forward-looking information.[129] Consequently, the safe harbor precludes securities issuers from civil liability if: 1) a forward-looking statement turns out to be wrong, as long as the statement is immaterial; or 2) the statement is material and "accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the forward-looking statement[.]"[130] Additionally, the safe harbor provision protects material statements made without the required cau-

125. *See* D'Alvia & Vulanovic, *supra* note 15 (describing Congress' reason for the addition of a safe harbor provision for forward-looking statements within the PSLRA).

126. *See* Andrew W. Fine, *A Cautionary Look at a Cautionary Doctrine*, 10 BROOK. J. CORP. FIN. & COM. L. 521, 528–29 (2016) (explaining that commentators maintain that the PSLRA's safe harbor provision is a codified version of the common law's bespeaks caution doctrine because the two are "strikingly similar"); *see generally* 15 U.S.C. § 78u-5(c) (providing the statutory language that codifies the common law "bespeaks caution" doctrine).

127. "Issuers," as defined by the Securities Act of 1933, means "every person who issues or proposes to issue any security . . . ." Securities Act of 1933, § 2(a)(4); 15 U.S.C. § 77B(a)(4).

128. *See* Fine, *supra* note 126, at 531–32 (noting that both Congress and the courts have encouraged companies to be generous in their disclosures to encourage open communication and a restoration of the securities litigation system's integrity). The bespeaks caution doctrine is a judicially-created doctrine stating that forward-looking statements are not misleading if they adequately disclose risks that may impact the company's forward-looking predictions. *See id.* at 528–29. The doctrine is a "popular tool used by the courts when granting a motion to dismiss or a motion for summary judgment" in securities fraud cases. *Id.* at 528 (citing Anand Das, *A License to Lie: The Private Securities Litigation Reform Act's Safe Harbor for Forward-Looking Statements Does Not Protect False or Misleading Statements When Made with Meaningful Cautionary Language*, 60 CATH. U.L. REV. 1083, 1091 (2011)). Under this doctrine, the cautionary language accompanying a forward-looking statement must: (1) relate clearly and unambiguously to the statement; (2) be substantive and narrowly tailored to the statement; (3) "conspicuously accompany" the statement; and (4) provide enough information to put a "reasonable investor" on notice that the statement is a prediction. *Id.* at 531–32.

129. *See* Coates, *supra* note 26, at n.14 (citing H.R. REP. NO. 104-369, 43 (November 28, 1995) (noting that Congress created the safe harbor provision to "enhance market efficiency by encouraging companies to disclose forward-looking information").

130. 15 U.S.C. § 78u-5(c)(1)(A) (detailing the requirements that a forward-looking statement must meet to receive the safe harbor's protections).

tionary statements if the party who made those statements lacked actual knowledge that the statement was false or misleading.[131] Though these protections are broad, the safe harbor provision does not protect non-forward-looking statements.[132]

Congress's inclusion of the safe harbor provision reflects a compromise between two competing interests: first, investor protection issues raised by forward-looking statements containing materially false information, and second, the need to encourage corporate disclosure and transparency.[133] Consequently, the safe harbor provision only protects those statements that strictly adhere to the stringent guidelines established within the provision.[134] Notably, the safe harbor provision's liability protection only applies in private litigation and does not prevent the SEC from pursuing appropriate enforcement action.[135]

4. *Exceptions to the Safe Harbor Provision*

The PSLRA's legislative history indicates that the safe harbor provision's protections were only meant for "seasoned issuers" with an "established track record."[136] Consequently, the safe harbor provision explicitly excludes any forward-looking statement made by or in connection with an offering of securities by a blank check company, a penny stock issuer, or an IPO.[137] These offerings tend not to have the "established track record"

131. *See id.* § 78u-5(c)(1)(B).

132. *See* Coates, *supra* note 26, at n.13 (noting that the safe harbor does not apply to statements made about to a company's current valuation, operations, or other non-forward-looking statements).

133. The PSLRA legislative history states:

> [The PSLRA] seeks to protect investors, issuers and all who are associated with our capital markets from abusive securities litigation. This legislation implements needed procedural protections to discourage frivolous litigation. It protects outside directors, and others who may be sued for non-knowing securities law violations, from liability for damage actually caused by others . . . [a]nd it establishes a safe harbor for forward-looking statements, to encourage issuers to disseminate relevant information to the market without fear of open-ended liability.

H.R. REP. NO. 104-369, at 32 (1995) (Conf. Rep.), *as reprinted in* 1995 U.S.C.C.A.N. 730, 731.

134. *See* 15 U.S.C. §§ 78u-5(c)(1)(A)–(B).

135. *See id.* § 78u-5(c)(1) (noting the limitations placed on the safe harbor's liability protections).

136. *See* Coates, *supra* note 26, at n.16; *see also* Matt Levine, *Money Stuff: Maybe SPACs Are Really IPOs*, BLOOMBERG (Apr. 12, 2021, 12:11 PM), https://www.bloomberg.com/news/newsletters/2021-04-12/money-stuff-maybe-spacs-are-really-ipos [https://perma.cc/C2VF-4HCT] (noting that the point of the safe harbor is to allow "regular established public companies" to tell shareholders about their future plans without fear of being sued, not to let to "let shady companies take advantage of the rule to spin wild tales and sucker people into investing").

137. Private Securities Litigation Reform Act of 1995, 15 U.S.C. §§ 77z–2(b)(1)(B)–(C), 2(b)(2)(D); *see also* Levine, *supra* note 136 (explaining that these specific types of transactions are excluded from the safe harbor because they pose too much risk of fraud or conflicts of interest).

of long-traded, public companies, thus excluding them from the safe harbor's protection.[138]

Congress explicitly defined blank check companies and penny stock issuers within the PSLRA but failed to provide any definition or guidance for the types of companies that fall within the IPO carve-out.[139] Presently, de-SPAC transactions do not fall within any of the safe harbor's defined carve-outs.[140] The PSLRA provides overlapping definitions for blank check companies and penny stock issuers; a blank check company is a company that plans to pursue a merger with an unidentified business *and* engages in the issuing of penny stocks.[141] This definition limits blank check companies to only those companies that issue penny stocks, effectively excluding SPACs from this carve-out.[142] In addition, most SPACs do not meet the PSLRA's trading requirements for companies that fall within the penny stock issuer carve-out; to be a penny stock issuer, the company must trade its shares for less than $5 per unit—SPACs typically trade at ten

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138. *See* Coates, *supra* note 26 (explaining that these blank check companies and penny stock issuers do not have an established financial or business history to support forward-looking projections, and thus, are excluded from the safe harbor provision).

139. *See id.* at n.15 (comparing the safe harbor's treatment of blank check companies and penny stock issuers to its treatment of IPOs, and establishing that under the PSLRA, most SPACs do not meet the blank check company definition).

140. *See id.*

141. *See* 15 U.S.C § 77z-2(i)(3) (defining "penny stock"); *see also* Offerings by Blank Check Companies, 17 C.F.R. § 230.419(a)(2)(ii) (2006). Rule 419 defines a "blank check company" as a company that:

> (1) is a development stage company that has no specific business plan or purpose or has indicated that its business plan is to engage in a merger or acquisition with an unidentified company or companies, or other entity or person; and
>
> (2) is issuing "penny stock," as defined in Rule 3a51-1 under the Securities Exchange Act of 1934 . . .

Id.; *see also* Coates, *supra* note 26, at n.15 (explaining that the PSLRA's exclusion for blank check companies overlaps the exclusion for penny stock issuers). Per the safe harbor provision, a "penny stock" is:

> [A]ny equity security other than a security that is registered . . . and traded on a national security exchange . . . authorized for quotation on an automated quotation system . . . issued by a [registered] investment company . . . excluded, on the basis of exceeding a minimum price . . . or exempted . . . by the [SEC].

15 U.S.C §§ 78c (51)(a)(i)–(v). Put another way, the SEC prescribes a specific definition to a penny stock: it is a share issued by a small company that is traded at a price below five dollars, that is usually traded over the counter (but can also be traded on exchanges). *See What is a Penny Stock?*, CORP. FINANCE INST., https://corporatefinanceinstitute.com/resources/knowledge/trading-investing/penny-stock/ [https://perma.cc/5VSW-MAZF] (last visited Apr. 11, 2022) (providing a brief explanation of the SEC's specific definition for "penny stock"). These shares are illiquid, and they can be difficult to price. *See id.*

142. *See* Coates, *supra* note 26, at n.15 (admitting that the SEC has not substantively amended the definition of "blank check company" since the passage of the PSLRA but may choose to do so in the future).

dollars a share.[143] Despite these explicit definitions, the safe harbor provision fails to provide any definition for the IPO carve-out—either within the PSLRA or by reference to another SEC rule.[144] For purposes of the PSLRA, "initial public offering" is not a technical term as it is not subject to a stringent definition like the blank check company and penny stock issuer carve-outs.[145] Thus, the PSLRA's ambiguity allows regulators to interpret the IPO exclusion to include de-SPAC transactions.[146]

III. IGNITION POINT: ALARM BELLS SOUND FOR INCREASED REGULATORY SCRUTINY OF THE DE-SPAC TRANSACTION

The recent flare-up in SPAC popularity came with a correlative rise in SPAC-related litigation in both state and federal courts.[147] SPAC-related litigation made up only one to two percent of all securities class action lawsuits filed in 2019 and 2020.[148] However, this number jumped to nearly fourteen percent of all securities class action lawsuits filed between January 1, and May 31, 2021.[149] Research has shown that much of this litigation arose in connection with the de-SPAC transaction, specifically in connection to the forward-looking statements made by sponsors to investors.[150]

Following the 2020 and early 2021 SPAC boom, it comes as no surprise that regulators are calling for increased scrutiny of SPACs, specifically, the de-SPAC transaction.[151] The SEC has signaled a renewed

143. *See What You Need to Know About SPACs*, *supra* note 16 (noting that SPAC sponsors typically price the SPAC's shares at a "nominal" $10 per unit); *see What is a Penny Stock?*, *supra* note 141 (explaining that the typical penny stock issuer is a small company that sells its shares at $5 a unit).

144. *See* Coates, *supra* note 26 (observing that in addition to the PSLRA's failure to provide or reference a definition, there is not any "relevant" case law that provides guidance on the types of companies that fall within this classification).

145. *See* Levine, *supra* note 136 (interpreting Coates' letter to say that the PSLRA does not treat "initial public offering" as a technical term which means the category is not exclusively limited to traditional IPOs).

146. *See* Coates, *supra* note 26 (explaining that the ambiguous definition of IPOs under the PSLRA may include the de-SPAC transaction).

147. *See* Glen Kopp, Glenn Vanzura & Jason Linder, *Mitigating SPAC Enforcement and Litigation Risks*, HARV. L. SCH. F. ON CORP. GOVERNANCE (May 18, 2021), https://corpgov.law.harvard.edu/2021/05/18/mitigating-spac-enforcement-and-litigation-risks/ [https://perma.cc/L3UF-VZHP] (detailing the dramatic increase in SPAC-related litigation cases over the past three years).

148. *See* CHO, *supra* note 64 (finding that the number of SPAC-related litigation cases filed in 2019 and 2020 compared to those filed in the first five months of 2021 had increased by nearly twelve percent).

149. *See id.*

150. *See* Kopp et al., *supra* note 147 (finding that most SPAC-related litigation risk stems from the potential for lawsuits filed in connection with the de-SPAC transaction).

151. *See* Nikolai Roussanov, *Why SPACs Are Booming*, KNOWLEDGE WHARTON (May 4, 2021), https://knowledge.wharton.upenn.edu/article/why-spacs-are-booming/ [https://perma.cc/X8SQ-7XJD] (providing background to the increased regulatory scrutiny that SPACs are experiencing).

enforcement interest in SPACs.[152] John Coates, former Acting Director of the SEC's Division of Corporate Finance, recently highlighted the "significant investor protection concerns" raised by the claim that SPACs are included within the PSLRA's safe harbor provision and are thus subject to lesser securities law liabilities than a traditional IPO.[153] Coates posited the idea that the de-SPAC transaction may be an IPO transaction in disguise, calling into question the validity of the claim that the transaction is granted the safe harbor's protection.[154] This is not the first time an SEC official has highlighted investor protection concerns raised by forward-looking statements in the de-SPAC transactions.[155]

A. *Striking the Flint: Early Signaling from Regulators*

In September 2020, SEC Chairman Jay Clayton commented that the SEC was taking a closer look at SPAC disclosure requirements.[156] Specifically, the Chairman drew attention to sponsors' incentives to complete a de-SPAC transaction and the compensation associated with it.[157] Chairman Clayton noted that SPACs could be a "very healthy" alternative to the

152. *See id.* (outlining the SEC's renewed interest in SPAC governance).

153. Coates, *supra* note 26 (listing some of the investor protection concerns raised by the proposition that the de-SPAC transaction receives the PSLRA's protections from civil liability).

154. *Id.* (questioning whether the de-SPAC transaction is actually an IPO and thus subject to the IPO carve-out of the safe harbor); *see also* Roussanov, *supra* note 151 (providing coverage of John Coates letter and the potential investor protection concerns raised by the current lack of regulatory oversight for the de-SPAC transaction).

155. *See* Dave Michaels & Alexander Osipovich, *Blank-Check Firms Offering IPO Alternative Are Under Regulatory Scrutiny*, WALL ST. J. (Sept. 24, 2020, 4:34 PM), https://www.wsj.com/articles/blank-check-firms-offering-ipo-alternative-are-under-regulatory-scrutiny-11600979237 [https://perma.cc/3APF-22FM] (examining SEC Chairman Jay Clayton's comments pertaining to heightened regulatory scrutiny of SPACs and the comments' impact on the market); *see also What You Need to Know About SPACs, supra* note 16 (providing investors a brief explanation of SPACs and potential areas of concern); *see also Staff Statement on Select Issues Pertaining to Special Purpose Acquisition Companies*, SEC (Mar. 31, 2021), https://www.sec.gov/news/public-statement/division-cf-spac-2021-03-31 [https://perma.cc/48A8-CG57] [hereinafter *Staff Statement on Select Issues*] (providing guidance for private companies participating in a de-SPAC transaction, specifically addressing reporting issues that should be addressed); *see also CF Disclosure Guidance: Topic No. 11* (Dec. 22, 2020) SEC, https://www.sec.gov/corpfin/disclosure-special-purpose-acquisition-companies [https://perma.cc/66TQ-WY6J] [hereinafter *CF Disclosure Guidance*] (providing guidance about disclosure considerations that sponsors should take into consideration during the SPAC's IPO and de-SPAC transaction).

156. *See* Michaels & Osipovich, *supra* note 155 (referencing Chairman Jay Clayton's comments that the SEC is looking into how SPAC sponsors disclose their ownership interests and how any compensation they receive is tied to an acquisition).

157. *See id.* Chairman Clayton summarized his concerns in an interview with CNBC, stating, "One of the areas in the SPAC space I'm particularly focused on, and my colleagues are particularly focused on, is the incentives and compensation to the SPAC sponsors." *Id.* Further, he added, "How much of the equity do they

traditional IPO. However, he noted that this is dependent on "whether investors are getting all the information [that] they need."[158] These comments highlighted the SEC's renewed interests in SPACs and the discussion surrounding enhanced disclosure requirements for sponsors.[159]

In early 2021, SEC Commissioner Hester Peirce signaled an interest in enhancing disclosure requirements for SPACs, stating, "We should ensure SPACs are providing sufficient disclosures to enable informed investment decision-making at each stage."[160] Additionally, the SEC has taken more subtle steps to warn investors of the potential risks imposed by SPACs, including providing official guidance on disclosure considerations related to a sponsor's conflicts of interest, as well as disseminating investor alerts and bulletins to increase public awareness about the potential risks associated with investing in SPACs.[161] In March 2021, the SEC took these concerns to the next level when it launched an informal investigation that scrutinized the SPAC dealings of numerous Wall Street Banks.[162] Finally, the new Chairman of the SEC, Gary Gensler, signaled that SPACs will be an area of increased focus and enforcement during 2021 and beyond.[163]

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have now? How much of the equity do they have at the time of the IPO-like transaction? What are their incentives?" *Id.*

158. Katanga Johnson, *Top U.S. Markets Watchdog Says Blank-Check IPOs Offer 'Healthy Competition'*, REUTERS (Sept. 24, 2020, 10:32 AM), https://www.reuters.com/article/us-usa-sec-clayton-spac/top-u-s-markets-watchdog-says-blank-check-ipos-offer-healthy-competition-idUSKCN26F2II [https://perma.cc/6HH5-DLGT] (quoting SEC Chairman Jay Clayton's September 2020 comments pertaining to SPACs).

159. *See* Michaels & Osipovich, *supra* note 155 (noting that Chairman Clayton's comments were "intended to communicate that regulators are closely reviewing SPAC written disclosures," not to indicate enforcement action); *see also* Kopp et al., *supra* note 147 (indicating that SEC officials have "signaled a renewed enforcement interest in SPACs").

160. Commissioner Hester M Peirce, Remarks at Investor Advisory Committee Meeting (Mar. 11, 2021), https://www.sec.gov/news/public-statement/peirce-statement-investor-advisory-committee-meeting-031121 [https://perma.cc/L68J-6825].

161. *See id.*; *see also What You Need to Know About SPACs*, *supra* note 16 (alerting investors to potential areas of concern throughout the SPAC process); *see also Staff Statement on Select Issues*, *supra* note 155; *CF Disclosure Guidance*, *supra* note 155 (addressing disclosure considerations throughout the SPAC process, specifically the SPAC's IPO and its business combination transaction); *see also Celebrity Involvement with SPACs—Investor Alert*, *supra* note 92 (warning investors about the dangers of making investor decisions based solely on celebrity participation or recommendation).

162. *See* Kopp et al., *supra* note 147 (explaining active steps that the SEC has taken to ramp up regulatory scrutiny of SPACs). Reportedly, the SEC requested that the banks volunteer information pertaining to "SPAC deal fees and volumes, as well as their compliance, reporting, and internal control functions related to such deals." *See id.*

163. *See id.* (providing coverage of Commissioner Gensler's 2021 Enforcement Agenda).

B. *Combustion: John Coates' Explosive Letter*

On April 8, 2021, Former Director Coates issued a public statement pertaining to SPACs, IPOs, and associated liability risks under federal securities laws that sent shockwaves throughout the financial industry.[164] Though Coates posited a neutral stance, neither pro- nor anti-SPAC, his message was clear: the SEC is "continuing to look carefully at filings and disclosures by SPACs and their private targets" and cautioned that "[a]ny simple claim about reduced liability exposure [under the safe harbor provision] for SPAC participants is overstated at best, and potentially seriously misleading at worst."[165] Most notably, Coates challenged the prevailing notion that the de-SPAC transaction, compared to traditional IPOs, significantly lowered liability exposure under securities laws.[166] Further, Coates argued that the de-SPAC transaction could be treated as the "real IPO," which would subject the transaction to the "full panoply of federal securities law protections . . . ."[167] Consequently, Coates stressed that any material misstatements in, or omissions from, registration statements or proxy disclosures in connection with a SPAC IPO or de-SPAC transaction could give rise to securities law violations.[168] Finally, the public statement drew into question the prevailing argument that the PSLRA afforded SPAC transactions benefits that it withheld from traditional IPOs, stating that the explicit exclusion of traditional IPOs from the safe harbor may extend to the de-SPAC transaction.[169]

164. *See* Coates, *supra* note 26; *see also* Anirban Sen, Chris Prentice & Joshua Franklin, *Exclusive: U.S. Watchdog Mulls Guidance to Curb SPAC Projections, Liability Shield—Sources*, REUTERS (April 27, 2021, 3:16 PM), https://www.reuters.com/article/us-usa-sec-exclusive-idTRNIKBN2CE2IM [https://perma.cc/8R4S-XDUX] (positing that the increased regulatory scrutiny could be the reason that the SPAC market started to cool down in April 2021).

165. *See* Coates, *supra* note 26 (warning investors and SPAC sponsors about the potential liability risks associated with overstating reduced liability exposure to investors but commenting that he was neutral towards SPACs); *see* Sen et al., *supra* note 164 (noting that despite Coates' neutrality claims, the SEC has significantly stepped up its scrutiny of SPACs, which has had an effect on markets).

166. *See* Coates, *supra* note 26 (challenging the notion that SPACs, specifically the de-SPAC transaction, are subject to lesser securities law liability because they are not a traditional IPO).

167. *See id.* (arguing that the de-SPAC transaction may actually be the "real IPO" of the SPAC process because a company with established operations is selling its shares to the public for the first time, thus subjecting the transaction to securities law liabilities for unfounded forward-looking statements).

168. *See id.*

169. *See id.* (explaining that the nature of the de-SPAC transaction, a transaction that brings a private operating company public, is reminiscent of the widely accepted traditional IPO process, and may be subject to the same exceptions that traditional IPOs face).

IV. WHERE'S THE FIRE EXTINGUISHER? REGULATORS MUST STEP IN TO PROTECT INVESTORS

The PSLRA's safe harbor provision grants public companies protection from liability for certain forward-looking statements made within their proxy statements.[170] In doing so, Congress recognized the important role forward-looking statements have in an investor's decision-making process.[171] However, Congress was rightfully skeptical of the trustworthiness of forward-looking statements made in connection with a private company's IPO.[172] Undoubtedly, this is why traditional IPOs are excluded from the safe harbor provision; they simply do not have the established track records or reporting histories that public companies have to back their projections.[173] This is evidenced by the internal conversation surrounding the passage of the PSLRA, where Congress agreed that the safe harbor provision applied to "seasoned issuers" with an "established track record" rather than unproven IPOs.[174] The recent SPAC boom has highlighted an enormous loophole in the PSLRA's safe harbor: the investment vehicle reportedly allows an unproven private company, with no established track record or market performance data, to go public while including forward-looking statements in its proxy statements, i.e., the equivalent of an IPO's prospectus.[175] Allowing SPACs and SPAC sponsors to continue to take advantage of these loopholes creates significant investor protection concerns, highlighting the need for regulators to step in and address the IPO carve-outs ambiguity.[176]

170. *See* Fine, *supra* note 126, at 522–23 (providing that the safe harbor grants public companies "conditional legal immunity" for forward-looking statements that are accompanied by "meaningful cautionary language").

171. *See* Coates, *supra* note 26 (explaining that forward-looking statements can be an important part in an investor's decision to invest in a company while highlighting the potential pitfalls this could have if the forward-looking statements are false or misleading).

172. *See* Michael Dambra, Omri Even-Tov & Kimberlyn George, *Should SPAC Forecasts Be Sacked?*, HARV. L. SCH. F. OF CORP. GOVERNANCE (Oct. 11, 2021), https://corpgov.law.harvard.edu/2021/10/11/should-spac-forecasts-be-sacked/ [https://perma.cc/4W2Y-HV5R] (asserting that Congress's skepticism of the validity of forward-looking statements made in connection with a firm's IPO motivated the exclusion of such statements from the safe harbor provision).

173. *See* INVESTOR BULLETIN, *supra* note 8, at 2 (explaining that the company going public through a traditional IPO typically lacks a prior reporting history, which is relied on by investors to inform their investment decision, thus requiring them to rely on the information provided within the prospectus).

174. *See* Coates, *supra* note 26, at n.16 (quoting the statement of Senator Diane Feinstein, who said, "The provisions [of the PSLRA] are only available to companies with an established track record," and "I understand the safe harbor does not apply to a new company, but only applies to seasoned issuers.").

175. *See* Dambra et al., *supra* note 172, at 10–11 (establishing that SPACs allow private companies to avoid the liability imposed on traditional IPOs under the PSLRA).

176. *See* Coates, *supra* note 26 (suggesting that the SEC disagrees with the assertion that SPACs are subject to lesser securities law liability, instead positing that the de-SPAC transaction is subject to the same restrictions as a traditional IPO

A. *Adding Fuel to the Fire: SPAC Sponsors Have a Unique Incentive to Exaggerate Forward-Looking Statements in the De-SPAC Transaction*

SPAC sponsors, target companies, and other interested parties assert that the de-SPAC transaction falls within the PSLRA's safe harbor, thus allowing sponsors to include forward-looking projections in the de-SPAC transaction's proxy statements.[177] However, this assertion fails to account for SPAC sponsors' significant financial incentive in ensuring that a de-SPAC transaction is achieved within the required timeframe.[178] SPAC sponsors typically receive a twenty percent stake in the merged company and a percentage of the value of the potential deal.[179] Before the SPAC and target company complete an acquisition, sponsors must convince shareholders to approve the merger agreement; without this approval, the deal fails.[180] To accomplish this, sponsors provide investors with forward-looking statements and projections as a part of the "acquisition narrative" used to convince shareholders to vote in favor of the proposed merger.[181] Additionally, investors rely on these projections to determine whether to sell their SPAC shares prior to the merger, or transfer their shares to the newly combined company.[182] In this situation, SPAC sponsors are again tasked with convincing shareholders that the combined company is a sound investment, thus creating incentive for the sponsors to exaggerate financial projections.[183] Consequently, sponsors' significant financial stake in the completion of the de-SPAC transaction incentivize untested

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to ensure investors are protected from over-zealous forward-looking statements made by SPAC sponsors).

177. *See id.* (outlining SPAC proponents' arguments that the de-SPAC transaction falls within the PSLRA's safe harbor provision for forward-looking statements).

178. *See* Carroll et al., *supra* note 28 (positing that SPAC sponsors' financial incentives encourage them to over-promise in forward-looking financial statements to complete the de-SPAC transaction).

179. *See* Huddleston, *supra* note 69 (providing that SPAC sponsors receive up to a twenty percent stake in the merged company, as well as a percentage of the potential profits); *see also SPACs Explained*, *supra* note 69 (citing CFA Society Chicago's Education Advisory Group) (explaining that SPAC managers commonly receive around five percent of the value of a potential deal).

180. *See* Aswath Damodaran, *Disrupting the Disruptors? The "Going Public Process" in Transition*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Oct. 29, 2021), https://corpgov.law.harvard.edu/2021/10/29/disrupting-the-disruptors-the-going-public-process-in-transition/ [https://perma.cc/9AQF-X96L] (explaining that in most de-SPAC transactions, SPAC sponsors must approve the merger agreement before the companies can carry out the de-SPAC transaction).

181. Dambra et al., *supra* note 172, at 2 (explaining that forward-looking statements are heavily relied upon by SPAC sponsors to solicit investor approval of a proposed merger).

182. *See id.* at 20–23 (positing that less sophisticated retail investors are drawn to forward-looking statements and base their investment decisions on them, thus concluding that these investors are more susceptible to being misled by such statements).

183. *See* Ramkumar, *supra* note 87 (explaining that sponsors transfer their SPAC shares, which were bought at a "deep discount," to the newly merged com-

and overly generous forward-looking statements to maintain shareholder support and approval of the de-SPAC transaction.[184]

B. *Fanning the Flames: SPACs Provide a Loophole for Private Companies to "Go Public" and Make Forward-Looking Statements*

SPAC proponents claim that the investment vehicle offers one major advantage to the traditional IPO: lesser exposure to securities law liability than a traditional IPO.[185] These proponents argue that SPACs, unlike traditional IPOs, may include forward-looking financial projections in proxy statements during the de-SPAC transaction without worrying about liability if the statements turn out to be false.[186] This argument tends to overlook the apparent similarities between the de-SPAC transaction and the traditional IPO.[187] Both the de-SPAC transaction and traditional IPO bring a private company to the public market, have the shared goal of transitioning an existing company from private to public ownership, and hope to raise capital for the newly public company.[188] The critical point here is that both transactions offer an avenue for private companies—without an established reporting history—to sell their shares to the public for the first time.[189] Despite these similarities, the two investment vehicles

pany during the de-SPAC transaction, resulting in a significant return on investment).

184. *See id.* (asserting that sponsors' ability to purchase up to twenty percent of a SPAC's shares at a deeply discounted price at the SPAC's IPO means that they will benefit from a de-SPAC transaction, even if the public company struggles and investors end up losing money).

185. *See id.* (presenting SPAC proponents claim that the de-SPAC transaction falls within the safe harbor's protections, which would grant it protection from civil liability for forward-looking statements that do not come to fruition); *see, e.g.*, Bazerman & Patel, *supra* note 85 (advancing the claim that SPACs offer target companies specific advantages over other forms of funding, namely IPOs, including higher valuation and fewer regulatory demands); Huddleston, *supra* note 69 (asserting that SPACs are advantageous to IPOs because they significantly reduce the time consumed by an IPOs registration process with the SEC); Domonoske, *supra* note 7 (proposing that the required disclosures for de-SPAC transactions are easier than IPOs because the SPAC does not have any business operations to describe).

186. *See* Levine, *supra* note 136 (explaining that it is "approximately" true that a company participating in a de-SPAC transaction can provide investors with its financial projections, whereas a company going through a traditional IPO is barred from doing so).

187. *See id.* (illustrating the similarities between the traditional IPO and de-SPAC transaction, while noting that SPACs are a "regulatory arbitrage" to the safe harbor's IPO carve-out).

188. *See* Ashford & Schmidt, *supra* note 105 (explaining that the purpose of an IPO is to bring a company public in order to raise funds for further investment into the company); *see also* Layne et al., *supra* note 25 (noting that SPACs are popular investment vehicles for private companies to raise additional capital, provide shareholders with liquidity, and pursue public ownership).

189. *See* Levine, *supra* note 136 (comparing the traditional IPO process to the de-SPAC transaction and concluding that similar to the traditional IPO, the de-SPAC transaction both brings a private company to the public markets and raises

receive significantly different treatments under the PSLRA.[190] Consequently, SPAC sponsors have seized this loophole, raising significant investor protection concerns—mainly, that investors are relying on forward-looking statements that are heavily based on predictions, not historical data.[191]

Congress created the safe harbor to encourage companies with an established reporting record to make forward-looking projections, not unproven companies making their market debut in an IPO or de-SPAC transaction.[192] SPACs often target start-up companies to merge with.[193] These companies attribute a large portion of their valuation to expected future financial growth, projected revenue, and anticipated profitability; these projections are speculative at best, as they are not based on previous financial records or market performance.[194] For example, if a company merges with a SPAC in a de-SPAC transaction, the combined company can market its initial public offering to investors based on projected future revenue and income; a traditional IPO may only provide investors with the company's past financial results.[195] This double standard encourages rela-

additional capital); *see also* Coates, *supra* note 26 (suggesting that the "economic essence" of an IPO is the introduction of a new company to the public).

190. *See* D'Alvia & Vulanovic, *supra* note 15 (explaining that SPACs essentially reverse the traditional IPO procedure, but forward-looking statements in the de-SPAC transaction are subject to different regulatory standards than the traditional IPO).

191. *See* Coates, *supra* note 26 (raising potential investor protection issues posed by allowing SPACs to include forward-looking statements in the de-SPAC transaction).

192. *See id.* at n.16. For a description of the legislative history and Congressional justifications for the PSLRA safe harbor provision, see *supra* notes 107–13 and accompanying text.

193. *See* Bazerman & Patel, *supra* note 85 (noting that SPACs are attractive to start-up companies as a way to go public because they can be customized to a number of different merger structures, and SPACs often offer higher valuations for these untested companies than a traditional IPO); *see also* Eliot Brown, *Electric-Vehicle Startups Promise Record-Setting Revenue Growth*, WALL ST. J. (Mar. 15, 2021, 5:30 AM), https://www.wsj.com/articles/electric-vehicle-startups-promise-record-setting-revenue-growth-11615800602 [https://perma.cc/VS5P-DKGW] (explaining that the start-ups that go public through SPACs are able to take advantage of the regulatory loophole found within the safe harbor because the transaction is currently viewed as a merger, not an offering).

194. *See* Levine, *supra* note 136 (illustrating the dilemma faced by "relatively immature, pre-revenue" companies trying to go public). Levine provided the following example to illustrate his point:

> If you are, say, an electric-vehicle company with some good ideas and smart engineers but no actual revenue, or cars, it is much more pleasant to tell investors how much money you plan to make in 2024 (lots) than it is to tell them how much money you made in 2020 (zero, or realistically a very negative number[ ]).

Id.

195. *See id.* (noting that at the moment, companies going public via a de-SPAC transaction can market themselves to investors based on projected future income, while companies going public via a traditional IPO are required to rely on past financial and performance results); *see* Brown, *supra* note 193 (detailing

tively immature companies—which have little to no revenue or reporting history—to bypass the traditional IPO requirements and instead pursue a merger with a SPAC, which allows the combined company to market itself using financial projections, not performance records.[196]

Regardless of one's stance on the de-SPAC transactions' securities law liability, it is clear that the traditional IPO and de-SPAC transaction share a common goal: introducing a private operating company to the public for the first time as a means of raising revenue and capital for the organization.[197] The PSLRA excludes traditional IPOs from the safe harbor provision to protect investors from "any dodgy little company" going public and making unreliable statements without the fear of being sued if they turn out to be wrong.[198] Unfortunately, SPACs exploit the safe harbor loophole and typically target companies that are not mature enough to positively perform on the public markets.[199] Without the built-in protections that traditional IPOs face—like required comprehensive regulatory disclosures and due diligence—it is nearly impossible for inexperienced investors to ascertain which offerings are a "dud."[200]

The safe harbor's IPO carve-out provides much-needed investor protections by barring companies without the requisite reporting history from

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critic's concerns that "inherently speculative" forward-looking statements contribute to the "hype" SPAC mergers receive compared to traditional IPOs).

196. *See* Osipovich & Michaels, *supra* note 5 (describing the allure of SPACs for immature companies as a way to bypass the cumbersome and expensive traditional IPO process, as well as highlighting the investor protection concerns that this raises).

197. *See* Ashford & Schmidt, *supra* note 105 (noting that a private company pursues a traditional IPO to raise funds for further investment into the company by allowing the public to purchase shares in the company, thus changing the company from private to public ownership); *see also* Layne et al., *supra* note 26 (commenting on the popular use of SPACs to bring a private company to the public markets).

198. *See* Levine, *supra* note 136 (positing that without the safe harbor's IPO carve-out, retail investors would be taken advantage of by companies who make "ridiculous" projections).

199. *See* Buhayar et al., *supra* note 61 (presenting critics' arguments that SPAC targets aren't ready for the public markets); *see also* Eliot Brown, *EV Companies Went Public with Big Plans. They're Quickly Hitting Snags.*, WALL ST. J. (last updated Apr. 2, 2021, 8:10 AM), https://www.wsj.com/articles/ev-companies-went-public-with-big-plans-theyre-quickly-hitting-snags-11617365407 [https://perma.cc/T6L3-PUC7]. One analyst stated to the *Wall Street Journal*, "These companies are finding it is harder to actually take that PowerPoint slide and get a product out of it than was envisioned." Id. The analyst questioned, "If you're having to reposition or pivot already, what's going to happen in three years or five years?" *Id.*

200. Buhayar et al., *supra* note 61 (explaining that SPACs that went on to merge with a target company saw their stocks fall on average 9.9% following the merger); *see Brown*, *supra* note 200 (illustrating the plight of private companies that go public through a SPAC by specifically pointing to four electric car companies whose sponsors made overzealous promises and projections during the de-SPAC transaction, which have failed to come to fruition, prompting sponsors to "reposition and pivot" less than a year after the de-SPAC transactions brought the private companies public).

including forward-looking statements within their proxy statements; the next logical step is to recognize the de-SPAC transaction as the initial public offering that it is.[201] As Coates suggests, "initial public offering" is not a technical term under the PSLRA—it does not have to refer to what is usually thought of as a traditional IPO.[202] Thus, the de-SPAC transaction, which is marketed as a merger between two companies, is more accurately described as an IPO, as it brings a private company public for the first time.[203] Accordingly, the de-SPAC transaction should be included under the safe harbor's IPO carve-out to protect investors from predatory forward-looking statements.[204]

V. Up in Smoke? Investors Will Be Burned if Regulators Don't Douse the Flames

If regulators fail to include the de-SPAC transaction in the safe harbor's IPO carve-out, investors will continue to fall victim to unsupported or overzealous forward-looking statements, and SPAC-related litigation will continue to rise.[205] Despite the important role forward-looking statements play in an investor's decision-making process, one cannot overlook the implied investor protections and reduction of class action securities lawsuits that including the de-SPAC transaction under the IPO carve-out would have.[206] There is broad consensus among the investment commu-

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201. *See* Coates, *supra* note 26 (positing that the de-SPAC transaction may *already* be included under the PSLRA's ambiguous definition for "initial public offering"); *see also* Carroll et al., *supra* note 28 (noting that the practical effects of Coates' argument is that federal judges should hold the de-SPAC merger as an IPO under existing law, thus excluding the de-SPAC transaction from the safe harbor provision).

202. *See* Coates, *supra* note 26 (declining to assume that the conventional IPO is the only definition available for an "initial public offering").

203. *See What You Need to Know About SPACs*, *supra* note 16 (explaining that despite a variety of ways to structure the business combination, the resulting company is a publicly traded company that carries on the target's business).

204. *See* Coates, *supra* note 26 (positing that the de-SPAC transaction should be excluded from the PSLRA's safe harbor provision for forward-looking statements because it shares the same goals as an IPO); *see also* Buhayar et al., *supra* note 61 (explaining that the de-SPAC transaction engages in an IPO when it brings a previously private company to the public market and offers initial shares to the market for public sale, and thus should be subject to heightened regulatory scrutiny).

205. *See* Lisa Silverman, *Guest View: SPAC Investors Face Six Key Risks*, REUTERS (May 13, 2021, 11:42 AM), https://www.reuters.com/breakingviews/guest-view-spac-investors-face-six-key-risks-2021-05-13/ [https://perma.cc/2DDD-6C8Y] (noting that lack of regulatory oversight of the de-SPAC transaction compared to traditional IPOs creates opportunity for fraud and risk to investors). The SPAC process is on a tight deadline, so sponsors often skip the necessary due diligence required in traditional IPOs, leading to inaccurate financial reporting, opportunities for material misstatements and omissions, unproven operations, inadequate controls, and conflicts of interest. *See id.*

206. *See* CHO, *supra* note 64 (positing that the risk of litigation could force sponsors to conduct a more thorough review of forward-looking statements to en-

nity that companies introduced through an IPO are too new and unpredictable for investors to rely upon their forward-looking statements.[207] Because of the material similarities between traditional IPOs and de-SPAC transactions, it is time to extend this protection to forward-looking statements made in conjunction with the de-SPAC transaction as a way to protect investors.[208] If regulators interpret the IPO carve-out to include these transactions, it would reshape the narrative surrounding SPACs and close a significant loophole that SPACs have taken full advantage of.[209]

This discussion now expands beyond the borders of investor advocates and financial regulators. On May 24, 2021, the U.S. House Committee on Financial Services received draft legislation that would amend the Securities Act and the Exchange Act to expressly exclude all SPACs from the PSLRA's safe harbor provision.[210] If this draft legislation becomes law, the amendment will subject SPAC sponsors to increased liability for inaccurate forward-looking statements made in connection to the de-SPAC transaction.[211] The legislation would accomplish this by changing the

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sure that they contain adequate cautionary language and sufficient disclaimers before they distribute them to investors).

207. *See* Levine, *supra* note 136 (explaining that the SEC's stance that companies brought public via an IPO are too new and lacking an established business record to make sound forward-looking projections, and that this view is nearly universally shared by legal counsel); Eric Reed, *What is an IPO and How Does it Work?*, THESTREET (Oct. 30, 2019), https://www.thestreet.com/markets/ipos/what-is-an-ipo-14763378 [https://perma.cc/RG2Q-PZPU] (explaining that traditional IPOs "have a tendency towards volatility" making them a risky investment for retail investors).

208. *See* Coates, *supra* note 26 (positing that current securities laws do not need to be amended to include the de-SPAC transaction within the safe harbor's IPO carve-out, but that these transactions are already included within the PSLRA's vague definition of "initial public offering").

209. *See* Miles Kruppa & Ortenca Aliaj, *A Reckoning for Spacs: Will Regulators Deflate the Boom?*, FINANCIAL TIMES (May 4, 2021), https://www.ft.com/content/99de2333-e53a-4084-8780-2ba9766c70b7 [https://perma.cc/6LLK-HB9S] (explaining that investor advocates claim that SPACs exploit the regulatory gap created by the PSLRA's vague language, and that increased regulatory scrutiny could have significant effects on SPAC markets and disclosure requirements).

210. *See* Ran Ben-Tzur & Jay Pomerantz, *House Releases Draft Legislation Eliminating SPAC Safe Harbor for forward looking Statements*, FENWICK & WEST LLP (June 7, 2021), https://www.fenwick.com/insights/publications/house-releases-draft-legislation-eliminating-spac-safe-harbor-for-forward-looking-statements [https://perma.cc/C9ER-4PTF] (providing that draft legislation has been introduced that would specifically exclude all SPACs from the PSLRA's safe harbor provision); *see also* D'Alvia & Vulanovic, *supra* note 15 (providing that the draft legislation is currently under review).

211. *See* Ben-Tzur & Pomerantz, *supra* note 210 (positing that the amendment would potentially create increased liability for inaccurate forward-looking statements made in conjunction with the de-SPAC transaction); *see also SPAC Update: Congress's Proposal to Eliminate Forward Looking Statement Safe Harbor for SPACs*, BAKER BOTTS (June 11, 2021), https://www.bakerbotts.com/thought-leadership/publications/2021/june/spac-update-congress-proposal-to-eliminate-forwardlooking-statement-safe-harbor-for-spacs [https://perma.cc/YXJ3-AKAD] (providing that the passage of this amendment may lead to increased liability risks for SPAC sponsors,

term "a blank check company" to "a development stage company that has no specific business plan or purpose or has indicated that its business plan is to acquire or merge with an unidentified company, entity, or person."[212] Additionally, in May 2021, SEC Chairman Gary Gensler reported to the House Appropriations Committee that the agency was creating new rules for SPACs, which are specifically targeted at protecting investors through increased transparency measures.[213] Further, in September 2021, a group of senators sent open letters to six influential SPAC founders inquiring about sponsor compensation and conflicts of interest posed by the SPAC's business combination.[214] The senators indicated that they were concerned about market integrity and protecting investors.[215] Though no formal action has been taken, it is clear that regulatory and legislative action is just around the corner, so SPAC sponsors and investors should pre-

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parties to the business combination agreement, and directors of the post-merger company).

212. *See* Barton & Ward, *supra* note 65 (citing *Virtual Hearing—Going Public: SPACs, Direct Listings, Public Offerings, and the Need for Investor Protections*, 117th Cong. 1 (2021)).

213. *See* Gary Gensler, *Testimony Before the Subcommittee on Financial Services and General Government, U.S. House Appropriations Committee*, SEC (May 26, 2021), https://www.sec.gov/news/testimony/gensler-2021-05-26 [https://perma.cc/RD93-BHUP] (explaining that the SPAC boom has put a lot of pressure on the agency's regulatory resources, while noting that the investment vehicle poses significant threats to investors, prompting discussion about creating new rules and guidance by the regulator).

214. *See* Letter from Elizabeth Warren, Sherrod Brown, Tina Smith, Chris Van Hollen, U.S. Senators, to Michael Klein, Founder and Managing Partner, M. Klein & Associates, Inc. (September 22, 2021), https://www.warren.senate.gov/imo/media/doc/SPAC%20letters%20[Combined].pdf [https://perma.cc/R7XV-JEFU]; Letter from Elizabeth Warren, Sherrod Brown, Tina Smith, Chris Van Hollen, U.S. Senators, to Stephen Girsky, Managing Partner, VectoIQ, LLC (September 22, 2021), https://www.warren.senate.gov/imo/media/doc/SPAC%20letters%20[Combined].pdf; Letter from Elizabeth Warren, Sherrod Brown, Tina Smith, Chris Van Hollen, U.S. Senators, to Tilman Fertitta, Chairman and CEO, Fertitta Entertainment, Inc. (September 22, 2021), https://www.warren.senate.gov/imo/media/doc/SPAC%20letters%20[Combined].pdf; Letter from Elizabeth Warren, Sherrod Brown, Tina Smith, Chris Van Hollen, U.S. Senators, to David T. Hamamoto, CEO & Chairman, DiamondHead Holdings Corp. (September 22, 2021), https://www.warren.senate.gov/imo/media/doc/SPAC%20letters%20[Combined].pdf; Letter from Elizabeth Warren, Sherrod Brown, Tina Smith, Chris Van Hollen, U.S. Senators, to Howard W. Lutnick, Chairman & CEO, Cantor Fitzgerald (September 22, 2021), https://www.warren.senate.gov/imo/media/doc/SPAC%20letters%20[Combined].pdf; Letter from Elizabeth Warren, Sherrod Brown, Tina Smith, Chris Van Hollen, U.S. Senators, to Chamath Palihapitiya, Co-Founder and CEO, The Social+Capital Partnership, L.L.C. (September 22, 2021), https://www.warren.senate.gov/imo/media/doc/SPAC%20letters%20[Combined].pdf.

215. *See id.* (explaining that "industry insiders" are using their position and knowledge to take advantage of "ordinary investors" throughout the de-SPAC process, which calls market integrity into question).

pare themselves for significant changes to the regulatory framework surrounding the entire SPAC process.[216]

It is high time to revisit the PSLRA's safe harbor provision for forward-looking statements.[217] The recent SPAC boom has heightened regulators' concerns about forward-looking statements made by sponsors in the de-SPAC transaction.[218] This comment proposes that the safe harbor's IPO carve-out should be interpreted to include the de-SPAC transaction as a way to combat growing investor protection concerns.[219] Regulators can expand these protections to the de-SPAC transaction because the safe harbor provision fails to provide or reference *any* definition for the types of offerings that constitute an IPO transaction under the PSLRA.[220] This proposal is based on the traditional IPO and de-SPAC transaction's shared goal: bringing a privately-held operating company public via an IPO.[221] Whether or not a de-SPAC transaction is included within the IPO carve-out, it is clearly a close substitute for the traditional IPO and should receive heightened scrutiny to protect investors from over-zealous sponsors.[222] The SPAC boom may have already happened, but regulators have a unique opportunity to douse the flames before more investors get burned. Only time will tell if they race to the scene and save the day.

216. *See* Barton & Ward, *supra* note 65 (warning SPAC sponsors, investors, and commentators of impending changes to the legislative and regulatory framework surrounding SPAC transactions and the forward-looking statements made in connection to the de-SPAC transaction).

217. For further development of this argument, see *supra* notes 170–204 and accompanying text (compelling regulators to turn their attention to the investor protection concerns raised by forward-looking statements in the de-SPAC transaction).

218. For a detailed discussion of regulator's concerns pertaining to forward-looking statements made in connection with the de-SPAC transaction, see *supra* notes 147–69 and accompanying text (outlining the shift in regulator's concerns about the de-SPAC transaction).

219. For further development of this argument, see *supra* notes 170–204 and accompanying text (urging regulators to reevaluate the liability associated with the de-SPAC transaction to protect investors from overzealous sponsors).

220. For a discussion of companies that fall within the respective carve-outs of the safe harbor provision, see *supra* notes 126–46.

221. *See* D'Alvia & Vulanovic, *supra* note 15 (noting that the SPAC process essentially flips the traditional IPO process around).

222. *See* Coates, *supra* note 26 (commenting on the material similarities of the traditional IPO and the de-SPAC transaction and suggesting that these similarities lend themselves to the conclusion that de-SPAC transactions should be included in the PSLRA's IPO carve-out).