

# SEC Speaks Out on SPACs, Highlights Legal Liability and Reporting Risks

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SPACs seem to be having their moment in the financial world, especially in 2021. In [less than three months](#), U.S.-based SPACs have raised more money – almost \$88 billion – than all SPACs combined in 2020 (which held the previous high for SPAC investment by some margin). They have even reached a level of societal notoriety, as shown by [this week's cover of New York Magazine](#). However, before SPACs and their supporters can carry this trend “[to the moon](#),” the SEC chose this week to release two notices bringing SPAC fans back to earth.

On April 8, Acting Director of the Division of Corporate Finance John Coates released a public statement titled “[SPACs, IPOs, and Liability Risk under the Securities Laws](#).” Coates notes that some commentators have argued SPACs present advantages over the traditional IPO process via “lesser securities law liability exposure for targets and the public company itself,” specifically the Private Securities Litigation Reform Act’s (PSLRA) safe harbor for forward-looking statements. While Coates admits projections are “woven into the fabric of business combinations,” he is concerned that “participants may not have thought through all the legal implications” of such statements. Rather, these claims of SPACs as the safer option are overstated at worst and may in fact pose greater liability “due in particular to the potential conflicts of interest in the SPAC structure.”

Under this approach on SPACs and their interaction with securities laws, Coates highlights that material misstatements or omissions in a registration statement are subject to liability under Section 11 of the Securities Act of 1933. Further, these types of classic securities missteps would also pose liability concerns when it comes to proxy solicitations and tender offers under Section 14 of the Exchange Act of 1934. These actions may also run afoul of state laws, which apply a duty of candor and fiduciary duties to these transactions when presented with potential conflicts of interest.

Notably, Coates explains how the PSLRA and its safe harbor may not be the shield its proponents expect it is. Excluded from this safe harbor are statements made in connection with a securities offering by a blank check company and those made in connection with an IPO. However, as the PSLRA does not define “IPO,” Coates theorizes that the deSPAC transaction is the true introduction of the economically viable company to the market and therefore the safe harbor would not apply to statements about such a transaction. In fact, it may not be a stretch to consider the entire SPAC lifespan – from IPO to deSPAC transaction – as part of the IPO for the purposes of liability and regulatory purposes.

On April 12, the Division of Corporate Finance again roiled the SPAC world by releasing a staff statement on [Accounting and Reporting Considerations for Warrants Issued by SPACs](#). In certain fact patterns examined by the Staff, the SEC found that SPACs may need to revise or restate historical financial statements with the SEC due to errors in the accounting treatment of warrants, a central feature of the SPAC structure. Warrants, commonly found in SPAC transactions, entitle a holder to purchase more stock at a later date (usually after the future SPAC target has been acquired). However, the SEC found several common practices – such as warrants that provided for potential changes to settlement amounts dependent on who held the warrant or scenarios whereby a tender offer would entitle warrant holders to cash while only certain common stock holders would be entitled to the same – would require the warrants not to be listed as equity but rather as “a liability measured at fair value.” By suggesting such errors would require financial restatements, the SEC is effectively forcing SPACs and deSPAC companies to take a closer look at their warrant offerings and SEC filings.

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In the coming days and weeks, we plan to post a deeper dive on these SEC statements and what they will mean for the SPAC litigation world. ***To stay up-to-date on events in the SPAC world, subscribe to Proskauer’s Corporate Defense and Disputes blog and we will keep you apprised of the latest developments.***

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