



Securities Law ADVISORY ■

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SEC Provides Guidance on Special Purpose Acquisition Company Disclosure Requirements

On December 22, 2020, the staff of the Division of Corporation Finance of the U.S. Securities and Exchange Commission (SEC) released [CF Disclosure Guidance: Topic No. 11](#) to assist special purpose acquisition companies (SPACs) to meet their disclosure obligations in connection with an initial public offering (IPO) or a business combination transaction.

Specifically, the guidance covers the disclosure considerations a SPAC should consider when drafting an IPO registration statement, including director, officer, sponsor, and underwriter conflicts of interest.

The guidance also covers disclosure considerations for SPACs engaging in a business combination or a “de-SPAC” transaction, including the disclosure of financing terms and the evaluation process for potential acquisition candidates.

In 2020, SPACs gained significant momentum in the market, and investors should be aware of the risks that come along with investing in a SPAC.

Initial Public Offering Disclosure Considerations

The guidance covers several disclosure topics registrants should consider when going through an IPO.

Conflicts of interest

SPAC sponsors, directors, and officers may not work exclusively on behalf of the SPAC to identify acquisition targets and may have fiduciary or contractual obligations to other entities. These arrangements and obligations may create conflicts of interest that should be disclosed.

The SEC instructed registrants to disclose the following:

- Any sponsors’, directors’, or officers’ potential conflicts of interest, including:
 - Any conflicts related to other business activities and whether they include fiduciary or contractual obligations to other entities.
 - How these activities may affect the sponsors’, directors’, or officers’ ability to evaluate and present a potential business combination opportunity to the SPAC and its shareholders.
 - How any potential conflicts will be addressed.

- Whether it is possible that the registrant will pursue a combination with a target in which the registrant's sponsors, directors, officers, or their affiliates have any interests.
- How the registrant will consider potential conflicts of interest.

Timeframe to close business combination transaction

SPACs generally commit to complete a business combination transaction within a specified timeframe. Under the typical terms of a SPAC's governing instruments, if the SPAC does not complete the transaction within that timeframe, it must liquidate and make a pro rata distribution to its public shareholders.

Registrants should consider the following disclosures as a SPAC nears the end of the specified timeframe:

- The financial incentives that SPAC sponsors, directors, and officers have to complete a business combination transaction, including how the incentives differ from the interests of public shareholders and quantification of the information about the losses the sponsors, directors, and officers would incur if the business combination transaction was not completed.
- The amount of control that SPAC sponsors, directors, officers, and their affiliates will have over approval of a business combination transaction.
- Whether the SPAC may amend the provisions in its governing instruments to facilitate the completion of the business combination transaction, including how the provisions would be amended, whether shareholder approval is required, what the voting standard for approval is, and whether the sponsors have sufficient voting power to approve it.
- Whether the SPAC may extend the time it has to complete the business combination transaction, including how the SPAC would extend the time and whether shareholders may redeem their shares in connection with any proposal to extend the time.
- Whether the sponsors, directors, officers, or their affiliates have prior SPAC experience, balanced disclosure about their prior experience, and the outcome of presented and complete business combination transactions and liquidations.

Underwriter deferred compensation

If the underwriter of the SPAC IPO defers its compensation until the closing of the business combination transaction, registrants should disclose the following:

- Whether the underwriter may provide additional services, such as identifying potential targets, providing financial advisory services, acting as a placement agent in a private offering, or underwriting or arranging debt financing, and any related fees.
- If the underwriter may provide additional services, the SPAC should include disclosure regarding:
 - A description of those potential services.
 - Fees the registrant may pay for those services.
 - Whether the registrant may pay those fees in other than cash.
 - Whether payment is conditioned on the completion of the business combination transaction.
 - Any conflicts of interest the underwriter may have in providing services given any deferred IPO underwriting compensation.

Economic terms of investments by sponsors, directors, officers, and their affiliates

The economic terms of the investments made by a SPAC's sponsors, directors, officers, and their affiliates usually differ from those of the public shareholders, which may create different financial incentives.

To reflect these potential differences, SPACs should disclose the following:

- What securities are owned by sponsors, directors, officers, and their affiliates; the price paid for the securities; a discussion of any concurrent offering of securities to the sponsors and their affiliates, including the amount of those securities and the price to be paid for those securities; and how the price of securities previously sold and currently offered to sponsors, directors, officers, and their affiliates compares to the public offering price in the IPO.
- A description of the conflicts of interest from the sponsors', directors', officers', and their affiliates' securities ownership, compensation arrangements, or relationships with affiliated entities that may create incentives to complete the business combination transaction.
- Whether the registrant's sponsors, directors, officers, and their affiliates are compensated for their services to the SPAC, including how they are compensated, whether any payments are contingent on the completion of the business combination transaction, and quantification of any known amounts of payments.

Terms of securities issued to sponsors

When a SPAC issues securities to its sponsors, the terms of those securities often differ from securities it issues to public shareholders. SPACs may also sell securities in private offerings, which also result in negotiated terms for those securities different from the shares sold in the IPO.

When this occurs, SPACs should consider the following disclosures:

- The terms of securities held by sponsors, directors, officers, and their affiliates, including how the rights of those securities compare to and differ from the rights and terms of securities offered in the IPO and the resulting risks to public shareholders.
- Whether the sponsors, directors, officers, and their affiliates hold convertible debt and, if so, the material terms of the conversion such as when the debt is convertible, the maximum number of securities they may acquire through conversion, and any contingencies on conversion.
- Whether the registrant plans to seek, or has obtained, additional funding. If there is going to be additional funding:
 - How the terms of the securities issued or to be issued in private offerings compares with the terms of the securities offered in the IPO.
 - Whether the sponsors, directors, officers, and their affiliates may participate in or have an interest in this financing.
- Whether the SPAC has entered into a forward purchase agreement allowing the purchaser to invest in the SPAC at the time of the business combination transaction. The disclosure must describe the terms of the agreement, any potential dilutive impact on other shareholders, and whether the forward purchaser's commitment to purchase the securities is irrevocable.

Business Combination Transaction Disclosure Considerations

The guidance covers topics registrants should consider when drafting a proxy statement or prospectus in preparation for a business combination transaction.

Financing disclosures

Registrants should consider whether additional financing disclosures are needed in connection with a business combination. The following information regarding financing should be disclosed:

- Any financing necessary to complete the business combination transaction.
- How the terms of the additional financing may impact public shareholders. If the terms of additional financing involve the issuance of securities, additional disclosure is required, including:
 - A description of how the price and terms of those securities compare to and differ from the price and terms of the securities sold in the IPO.
 - Whether sponsors, directors, officers, or their affiliates are participating in the additional financing.
- If issuing convertible securities, a description of the material terms for conversion and any material impact on the beneficial ownership of the combined company.

Potential acquisition disclosures

SPAC sponsors, directors, and officers often evaluate a number of potential acquisition candidates before presenting a business combination transaction to shareholders that may create conflicts of interests with public shareholders.

Given the potential for conflicts of interest, the following information about the evaluation, consideration, and approval of an acquisition target should be disclosed:

- Detailed description of the evaluation and decision-making processes used to propose the identified transaction, including:
 - How and why the registrant selected the target company.
 - Which party initiated contact.
 - The reasoning the target was selected over other potential candidates.
 - An explanation of the material terms of the transaction.
 - The process of the transaction for the private operating company.
 - A description of the negotiations for the nature and amount of consideration.
- A description of the material factors the board of directors considered in its determination to approve the identified transaction, including a description of how the board of directors evaluated the interests of sponsors, directors, officers, and their affiliates.
- A description of any conflicts of interest of the sponsors, directors, officers, and their affiliates in presenting this opportunity to the SPAC, including how the SPAC addressed any conflicts of interest. If a SPAC has a policy to address conflicts of interest and waived the policy, the waiver and the reasons for the waiver should be disclosed.

- Any interest the sponsors, directors, officers, or their affiliates have in the target operating company, including, if material, the approximate dollar value of the interest, when the interest was acquired, and the price paid for the interest.
- How the sponsors, directors, officers, or their affiliates will benefit from the transaction, including:
 - Whether any material payments they will receive as compensation or the return on their initial investment has been quantified.
 - Whether there are any continuing relationships they will have with the combined company.
 - The total percentage ownership interest the SPAC sponsors, directors, officers, and their affiliates hold in the combined company, including through the exercise of warrants and conversion of convertible debt.

Underwriter disclosures

Finally, if an underwriter of a SPAC IPO provides services in addition to those associated with the underwriting of the IPO and deferred a portion of its underwriting compensation until the closing of the SPAC's initial business combination transaction, the following information should be disclosed:

- The fees that the IPO underwriter will receive upon completion of the business combination transaction, including the amount of fees that is contingent upon completion of a business combination transaction.
- Any additional services the underwriter provided.
- The cost of the additional services the underwriter provided.
- How the underwriter and its affiliates were compensated for the services.
- Whether the services were conditioned on the completion of the business combination transaction.
- Any conflict of interest the underwriter may have had in providing such services given any deferred IPO underwriting compensation.

The SEC will expect these disclosures in SPAC IPOs and business combinations going forward, and SPACs and sponsors should anticipate these types of disclosures while setting up the transaction

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