

July 8, 2022

The Honorable Gary Gensler
Chair
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Dear Chair Gensler,

I write to express my strong support for the Securities and Exchange Commission's (SEC, the Commission) March 2022 proposed rules regarding special purpose acquisition companies (SPACs), which would enhance disclosures and investor protections in SPAC initial public offerings and de-SPAC transactions.¹ I appreciate your leadership in offering these proposals, which will level the playing field for retail investors and prevent Wall Street insiders from perpetuating scams and fraud to line their own pockets.

I have long been concerned about the risks SPACs pose for retail investors, and the fundamentally misaligned incentives between SPAC sponsors and investors. Following an extensive eight-month investigation into high-profile SPAC creators, I released the attached report highlighting issues of misaligned incentives, self-dealing, and fraud that plague the industry.² The findings of this report, based on information provided by SPAC creators, the SEC, and public disclosures, reveal the significant need for additional regulation from the Commission to bridge the information and access gap retail investors face in the SPAC industry.

The findings of the investigation, as outlined in the attached report, included:

- **SPAC Sponsors' Incentives and Outcomes Do Not Align with Retail Investors', Leading to Low-Quality Deals that Harm Investors.** The sponsor's "promote," a 20 percent share in the public company that sponsors pay a fraction of market value for, almost always guarantees a profit for sponsors, who frequently pay tens of thousands of dollars for hundreds of millions in stock.³ Since SPACs face time pressure to complete a merger – typically, money must be returned to investors and the SPAC must dissolve if a

¹ U.S. Securities and Exchange Commission, "SEC Proposes Rules to Enhance Disclosure and Investor Protection Relating to Special Purpose Acquisition Companies, Shell Companies, and Projections," press release, March 30, 2022, <https://www.sec.gov/news/press-release/2022-56>.

² Office of U.S. Senator Elizabeth Warren, "The SPAC Hack: How SPACs Tilt the Playing Field and Enrich Wall Street Insiders," May 2022, <https://www.warren.senate.gov/imo/media/doc/SPACS.pdf>.

³ New York Times, "Wall Street's New Favorite Deal Trend Has Issues," Andrew Ross Sorkin, February 10, 2021, <https://www.nytimes.com/2021/02/10/business/dealbook/spac-wall-street-deals.html>.

merger is not completed within two years – SPAC sponsors are incentivized to push low-quality deals to ensure they receive their promote.⁴ From 2019 to 2021, SPAC sponsors received average returns of 958 percent, even as companies taken public by SPACs consistently underperformed the market and retail investors took losses.⁵

- **SPAC Shortcuts Give Institutional Investors and Wall Street Insiders Profitmaking Opportunities that Dilute Shares for Retail Investors and Put Underlying Companies at Risk.** Wall Street insiders, including hedge funds and large financial institutions, are provided with various shortcuts throughout the SPAC process that are inaccessible to retail investors, including early access to information and discounted stock.⁶ In addition, these insiders are invited to participate in PIPEs, or private investments in public equity, that widen the information and access gap and practically guarantee insiders profits of up to 300 percent, while providing them with redemption rights that act as a “money-back guarantee.”⁷ These special favors for big investors dilute the value of retail investors’ purchases while reducing the capital available to the companies after they are taken public.
- **Financial Institutions Profit Off SPACs Through Hidden Fees that Outstrip Those of a Traditional IPO.** Financial institutions have benefited from the SPAC boom by charging various hidden fees that outstrip those of a traditional initial public offering (IPO), including an underwriter fee, a PIPE placement agent fee, and a financial advisor fee. According to information provided by high-profile SPAC underwriters,⁸ financial institutions that back SPACs received fees equal to 5.5-6 percent of the amount raised in the IPO, with a 2 percent underwriting fee at the closing of the IPO. In some cases, the company also received a capital markets advisory fee equal to 3.5 percent of the amount raised in the IPO and 5.5 percent of the over-allotment option.
- **SPACs Incentivize Inadequate and Even Fraudulent Disclosures.** Regulatory loopholes, lax requirements, and the misaligned incentives of the decision makers have created an environment where SPACs are rife with disclosures that border on or cross into outright fraud. In effect, SPACs have created a shortcut for private businesses to go public without the disclosure requirements of a traditional IPO. And because the SPAC sector is oversaturated and sponsors are incentivized to make a deal regardless of quality, there have been multiple cases where companies used inflated information about their financials, their future business, or even their underlying technology.⁹

⁴ *Id.*

⁵ New York Magazine, “The Big SPAC Crackdown,” Michelle Celarier, September 2, 2021, <https://nymag.com/intelligencer/2021/09/the-big-spac-crackdown.html>; Bloomberg, “Wall Street Is Churning Out SPACs at Investors’ Peril,” Noah Buhayar, Tom Maloney, and Zijia Song, November 16, 2021, <https://www.bloomberg.com/graphics/2021-what-is-a-spac-wall-street-investor-risk/>.

⁶ Bloomberg, “Wall Street Is Churning Out SPACs at Investors’ Peril,” Noah Buhayar, Tom Maloney, and Zijia Song, November 16, 2021, <https://www.bloomberg.com/graphics/2021-what-is-a-spac-wall-street-investor-risk/>.

⁷ Reuters, “High redemption rates see SPACs relying on alternative financing,” Roger E. Barton, January 14, 2022, <https://www.reuters.com/legal/transactional/high-redemption-rates-see-spacs-relying-alternative-financing-2022-01-14/>.

⁸ Office of U.S. Senator Elizabeth Warren, “The SPAC Hack: How SPACs Tilt the Playing Field and Enrich Wall Street Insiders,” May 2022, <https://www.warren.senate.gov/imo/media/doc/SPACS.pdf>.

⁹ *Id.*

- **SPACs Allow for Rampant Self-Dealing at the Expense of Retail Investors and the Health of the Market.** SPAC sponsors take advantage of the flaws in SPAC rules to benefit themselves in multiples steps of the process: paying advisory fees to companies they are associated with, participating in PIPEs and private investment rounds despite their clear insider knowledge, and even choosing their own companies as acquisition targets.

The proposed rules put forth by the Commission in March 2022 would address several of these imbalances. The Commission’s proposal to amend the definition of “blank check company” to remove the safe harbor in the *Private Securities Litigation Reform Act of 1995* for forward-looking statements would significantly curb SPAC sponsors’ abilities to make overblown and false projections, and increase their liability when this fraud occurs.¹⁰ In addition, the Commission’s proposed increase in disclosures, which would bring the requirements of a SPAC closer to those of a traditional IPO, would increase transparency regarding the fees and benefits SPAC sponsors, underwriters, and institutional investors receive.¹¹

Finally, I strongly support the Commission’s efforts to increase accountability for SPAC sponsors and underwriters following the de-SPAC transaction, both by deeming underwriters in the SPAC’s IPO as underwriters in the de-SPAC transaction, and by making the acquisition target a co-registrant in the de-SPAC transaction.¹² Clarifying the role of financial institutions and SPAC sponsors as underwriters in the de-SPAC transaction will give these parties an increased stake in the future of the merged company and open them up to liability from shareholders if the de-SPAC transaction includes undisclosed dilution or fraudulent statements.

Although the Commission’s proposed rules would significantly bridge the information gap between retail investors and SPAC sponsors, I encourage the Commission to continue pushing against the fundamentally misaligned incentives for stakeholders in this space. Our investigation found rampant fraud and self-dealing in the SPAC sector, and requiring additional disclosures on SPAC sponsors’, boards of directors’, and financial institutions’ potential conflicts of interest could give retail investors more transparency into the decision-making process. In addition, measures should be taken to prevent insiders from cashing out on SPAC deals before the merged company can succeed or fail, giving them more of a stake in the companies they profit off of. I am working to introduce legislation that would build on the Commission’s rules and expand the transparency and disclosure requirements to further protect retail investors.

It is not surprising that SPAC sponsors and insiders who have earned billions through this unfair scam are pushing back against the Commission’s proposed rules, with industry groups including the CFA Institute,¹³ the SPAC Association,¹⁴ and the American Securities Association¹⁵ submitting comment letters in opposition. The Commission should not accede to the concerns of

¹⁰ U.S. Securities and Exchange Commission, Federal Register Notice, “Special Purpose Acquisition Companies, Shell Companies, and Projections,” May 13, 2022, <https://www.federalregister.gov/documents/2022/05/13/2022-07189/special-purpose-acquisition-companies-shell-companies-and-projections>.

¹¹ *Id.*

¹² *Id.*

¹³ Letter from CFA Institute to the SEC, May 31, 2022, <https://www.sec.gov/comments/s7-13-22/s71322-20129959-296347.pdf>.

these special interests. The findings of our report reveal the need for significantly stronger rules to protect investors and the market, and show that the Commission's proposal would play an important role in addressing these problems.

Thank you for your hard work on this proposal, and for your attention to this matter.

Sincerely,



Elizabeth Warren
United States Senator

¹⁴ Letter from SPAC Association to the SEC, June 13, 2022, <https://www.sec.gov/comments/s7-13-22/s71322-20131123-301315.pdf>.

¹⁵ Letter from the American Securities Association to the SEC, May 27, 2022, <https://www.sec.gov/comments/s7-13-22/s71322-20130552-299410.pdf>.