SUING SPACS

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ABSTRACT

In 2020, the financial world became transfixed by a massive increase in the number of firms going public through special purpose acquisition company ("SPAC") transactions. A SPAC is a publicly traded company formed solely for the purpose of raising money from investors and choosing a merger partner, thereby bringing the target company public. SPAC shareholders vote on the proposed transaction, but also have the option to redeem their shares for the price paid plus interest prior to the merger. SPACs have always been controversial; they make risky ventures available to unsophisticated investors, may involve acute conflicts of interest, and do not make the rigorous disclosures required in standard IPOs.

Is litigation a solution to these problems? The SPAC boom, as many commentators predicted, precipitated a deluge of lawsuits. Although several studies examine the SPAC transactions themselves, this project is the first comprehensive study of SPAC-related litigation. Using a dataset of all SPAC transactions completed since 2014 and all SPAC-related lawsuits filed since 2017, I assess the prevalence and characteristics of these lawsuits. I find that the probability that a SPAC transaction will generate a lawsuit appears to be unrelated to the returns on the deal, the size of the merger, the industry of the target, and various proxies for SPAC quality. However, I find a negative association between the likelihood of litigation and redemption rate. This is surprising because it means that the SPAC transactions more likely to generate lawsuits are those in which the SPAC shareholders choose to keep, rather than redeem, their shares, presumably signaling greater

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confidence in the quality of the deal. I argue that many of these lawsuits are opportunistic and may be of questionable quality. I further argue that these lawsuits are an inadequate substitute for the liability that firms face in connection with standard IPOs.

TABLE OF CONTENTS

INTRODUCTION

Beginning in 2020, the financial world has been transfixed by a striking rise in the number of firms going public through special purpose acquisition company ("SPAC") transactions. Although SPACs have been in and out of vogue for several decades, the most recent explosion is unprecedented.[1] In 2020, 53% of all initial public offerings ("IPOs") were SPACs, and in the first quarter of 2021, that percentage rose to 62%,[2] when SPACs issued more than $30 billion per month in equity.[3]

A SPAC is essentially a publicly traded shell company whose sole purpose is to merge with a private company, thereby bringing it public. The SPAC raises money from investors in an IPO and has a limited period (often about two years) to search for a target. Once the SPAC identifies a merger partner, the target merges into the SPAC in a "de-SPAC" transaction, thus going public while itself avoiding the time-consuming and expensive IPO process. Upon the announcement of a merger, SPAC shareholders are given the opportunity to redeem their shares for the issuing price plus any interest accrued—usually about ten dollars. Low redemption rates are thought to signal confidence in the quality of the merger—shareholders think the transaction is a good one, and thus elect to retain their shares. High redemption rates, by contrast, may signal that shareholders and the market in general are skeptical of the deal.

SPAC transactions have been controversial for most of their existence. They allow young, risky firms to access the public markets—and potentially, unsophisticated investors.[4] De-SPAC transactions are conducted on tight

1. *See* Max H. Bazerman & Paresh Patel, *SPACs: What You Need to Know*, HARV. BUS. REV. July/Aug. 2021, at 104.

2. *Distribution of traditional IPOs and special purpose acquisition company (SPAC) IPOs in the United States from 2016 to 2021*, STATISTA (July 4, 2022), https://www.statista.com/statistics/1234111/number-traditional-spac-ipo-usa [https://perma.cc/YKA9-CYQA].

3. Ortenca Aliaj & Miles Kruppa, *The SPAC Machine Sputters Back to Life After Dramatic Meltdown*, FIN. TIMES (Nov. 21, 2021), https://www.ft.com/content/d1723a8e-c146-4d48-8475-01cc9947a5d6 [https://perma.cc/Z3ZF-CJN5]; *see also* John C. Coates, SPAC Law and Myths 2 (Feb. 11, 2022) (unpublished manuscript), https//ssrn.com/abstract=4022809 [https://perma.cc/7L32-9QEU].

4. Although recent studies have found that most investors in SPAC IPOs are institutional investors, *see* Michael Klausner, Michael Ohlrogge, & Emily Ruan, *A Sober Look at SPACs*, 39 YALE J. ON REG., 228, 298 (2022), they are known as "poor-man's private equity" because they allow the person on the street access to riskier, though potentially higher-reward transactions, *see* Usha Rodrigues & Michael Stegemoller, *Redeeming SPACs* 1 (Univ. of Ga. Sch. of L., Research Paper No. 2021-09, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3906196 [https://perma.cc/6DM8-B5HZ]. Commentators have also argued that retail investors may be more likely to lose out in de-SPAC transactions. *See* Bobby Reddy, *The SPACtacular Rise of the Special Purpose Acquisition Company: A Retail Investor's Worst Nightmare* 3 (Univ. of Cambridge Legal Stud., Research Paper No. 32/2021, 2021), http://ssrn.com/abstrat=3968983 [https://perma.cc/UV7A-M7DL].

timelines by management who will lose everything if the merger does not close. They may settle for subpar targets or terms, skimp on diligence, or even engage in outright fraud rather than risk losing a deal and returning all the IPO proceeds to the shareholders. Moreover, shareholders that see the transaction through face a risk of significant dilution that they may not understand.[5]

Is litigation a solution to these problems? It would not be crazy to think that surely the heightened risks that investors face in these transactions should be fully disclosed and that SPACs should face dire consequences if these disclosures are incomplete and inaccurate. But by design, the heavy hammer of strict liability under section 11 of the Securities Act and Exchange Act ("section 11"), which penalizes misstatements in standard IPOs, is generally inapplicable to SPACs. This has not deterred plaintiffs, however; top legal blogs[6] and press articles[7] began to bubble with anecdotal reports of a deluge of SPAC-related lawsuits in the spring of 2021. But while numerous commentators have examined the characteristics of the SPACs constituting the boom, so far there has been no comprehensive study of the litigation they have generated. What kinds of claims comprise this flood, and what is their role?

In a first attempt to answer this question, I analyze a sample of 230 SPAC transactions and 150 lawsuits (generated by 62 of those transactions). My sample encompasses the SPAC boom through the second quarter of 2021, which, by all accounts, seems to be the height of the frenzy. I find that the majority of claims arising from de-SPAC transactions are, perhaps unsurprisingly, so-called "merger objection" claims. These are brought either under state law, claiming violation of managers' fiduciary duties, or under section 14 of the Securities and Exchange Act, alleging fraud in the proxy materials by which management solicited shareholders to vote for the

5. Klausner et al., *supra* note 4, at 253.

6. *See, e.g.*, Douglas A. Rappaport, Jacqueline Yecies & Stephanie Lindmuth, *Recent SPAC Shareholder Suits in New York State Courts: The Beginning Wave of SPAC Litigation*, HARV. L. SCH. F. ON CORP. GOVERNANCE (Apr. 23, 2021), https://corpgov.law.harvard.edu/2021/04/23/recent-spac-shareholder-suits-in-new-york-state-courts-the-beginning-wave-of-spac-litigation [https://perma.cc/8ATG-7ZWH]; Ross Todd, *A Wave of SPAC Litigation is Coming. Here's What to Watch For*, AMLAW LITIG. DAILY (May 11, 2021), https://www.law.com/litigationdaily/2021/05/11/a-wave-of-spac-litigation-is-coming-heres-what-to-watch-for/?slreturn=20220917141038 [https://perma.cc/AVW4-EBJ6].

7. *See, e.g.*, Alison Frankel, *The New 'Deal Tax': SPAC Defendants Are Paying Plaintiffs Lawyers to Drop N.Y. State Suits*, REUTERS (May 5, 2021), https://www.reuters.com/business/legal/new-deal-tax-spac-defendants-are-paying-plaintiffs-lawyers-drop-ny-state-suits-2021-05-05 [https://perma.cc/8CMC-E7WK?type=image]; Kevin LaCroix, *Trouble Brewing in SPAC-Land?*, D&O DIARY (Apr. 13, 2021), https://www.dandodiary.com/2021/04/articles/securities-litigation/trouble-brewing-in-spac-land [https://perma.cc/W8BU-DMVS].

merger. Collectively, these merger objection claims comprise over 60% of the claims in my sample, and most are filed before the merger closes.[8] The second main class of claims comprising the SPAC litigation deluge are broader claims under Securities and Exchange Commission ("SEC") Rule 10b-5,[9] the all-purpose workhorse of securities litigation, which punishes material misstatements or omissions in connection with the purchase or sale of a security. These are typically brought after the closing of the de-SPAC transaction and comprise roughly 30% of the claims in my sample.[10]

Do these lawsuits target, improve, or deter bad SPACs? Although these lawsuits are in their early days, based on my sample, they appear in fact to target quite good SPACs. In examining these transactions and claims, my main finding is an intuitively odd one: that the likelihood that a de-SPAC transaction will generate a lawsuit—any kind of lawsuit—is negatively related to redemption rate. Transactions with higher redemption rates are commonly thought to be qualitatively worse mergers and might seem likely to generate more lawsuits. My sample, however, shows the reverse: that the probability that a transaction will generate litigation *rises* as redemption rates decline. This finding is robust to the inclusion of a panoply of controls. An equally puzzling finding is that based on my sample, the probability of being sued appears to be unrelated to deal size, target industry, returns of the merged company, managerial savvy, or various other proxies for deal quality.

What explains this surprising relationship between lawsuits and redemption rates? There are two potential explanations. One cheery possibility is that SPAC-related lawsuits may target fraudulent transactions in which misrepresentation by the management has had the effect of inducing investors to keep, rather than redeem their shares. If this is true, SPAC-related lawsuits may be fulfilling precisely the function for which they are designed: if brought after the merger, they are vindicating the interests of shareholders who did not redeem their shares because they were lied to. And if brought before the merger, these lawsuits may halt bad deals or prompt managers to improve transactions, thus inducing shareholders to keep their shares. If these stories are true, SPAC-related lawsuits are spectacularly successful and should be encouraged.

But there are also less rosy explanations for the negative relationship

8. I find 110 merger objection claims out of a total of 181 claims of the main types that I tabulate. *See infra* Table 3.

9. 17 C.F.R. § 240.10b-5. For simplicity, this Article will refer to this Rule as simply "Rule 10b-5."

10. There are 53 Rule 10b-5 claims out of 181 claims of the main types that I tabulate. *See infra* Table 3.

between litigation probability and redemption rate. Lower redemption rates—even if they legitimately signal a stronger transaction—could mean larger classes, more purported damages, and higher lawyers' fees, and may thus be tempting targets for lawsuits after the merger. And in the notoriously dysfunctional ecosystem of merger litigation, challenges to SPACs brought before the deal closes may be filed indiscriminately. Even more damning, they may target fraudulent transactions but *nonetheless fail to induce shareholders to redeem*. I argue that this is likely because these lawsuits are of low quality, as many merger challenges infamously are.[11] I find that the eventual returns on deals that generated merger objection claims are no better than those that did not, and all of the mergers in my sample closed. There thus appears to be no evidence that these lawsuits are improving de-SPAC transactions or weeding out the bad ones. Roughly half of the merger objection cases in my sample were voluntarily dismissed without litigation within the sample period. The few settlements that are publicly disclosed are for paltry fees. And they are generally filed prolifically and sloppily by a handful of entrepreneurial plaintiffs' firms composed of fewer than ten lawyers each.

The merger litigation in my sample is the product of a deliberate swap whereby SPACs substitute liability under the merger regime for the heavy cudgel of section 11 liability. In general, we are most concerned about misrepresentations precisely when firms are new to the market and have no history for shareholders to assess; this explains the rigidity of section 11 of the Securities Act, which provides virtually strict liability for misstatements and omissions in a registration statement, which firms file when they conduct an IPO. Because they are shells when they go public, SPACs have nothing to disclose in a registration statement and thus avoid exposure under section 11. To assess the effects of this "SPAC litigation swap," I compare pre-closing merger objection claims in my SPAC sample to section 11 claims in a sample of IPOs over the same period. I find that in substituting liability under the Securities Act for liability under the merger regime, SPACs have, in terms of sheer volume, fallen from the frying pan into the fire. The number of merger objection claims in 2020 and 2021 is equal to nearly 70% of the number of de-SPAC transactions (as opposed to less than 9% of the IPOs that drew section 11 claims across my sample). But while the merger challenges in my sample have so far disclosed only a few settlements with a mean of roughly $200,000, the mean section 11 settlement in my sample—

11. *See* Matthew D. Cain, Jill E. Fisch, Steven Davidoff Solomon & Randall S. Thomas, *The Shifting Tides of Merger Litigation*, 71 VAND. L. REV. 603, 604–05 (2018) [hereinafter Cain et al., *Shifting Tides*]; Matthew D. Cain, Jill Fisch, Steven Davidoff Solomon & Randall S. Thomas, *Mootness Fees*, 72 VAND. L. REV. 1777, 1777 (2019) [hereinafter Cain et al., *Mootness Fees*].

including cases that were dismissed or are ongoing—is roughly $4.5 million. All of this suggests that merger litigation, especially before the deal closes, may not perform the same policing function as section 11 liability. These cases are pervasive and cheap to settle, meaning that shareholders may not take them seriously as a signal of misconduct, and thus do not redeem their shares. Moreover, the penalties these lawsuits impose are likely too low to induce managers to be truthful.

If SPACs have problems in need of correction, it is unclear whether private litigation is up to the job. Pre-closing merger objection cases, which constitute much of the SPAC litigation deluge, seem to reflect an effort to collect many small fees for small plaintiffs' lawyers and are unlikely to result in better deals. And although their ultimate impact is unclear, even some lawsuits brought after the merger, largely under Rule 10b-5, may be calculated to procure a high fee for plaintiffs' counsel, rather than targeting true misconduct. If the SPAC structure constitutes a deliberate bargain by which public investors receive the opportunity to invest in potentially high-risk-high-reward ventures normally unavailable to them in return for less information, perhaps this is no cause for concern. On this view, SPAC litigation may be working as designed; expensive section 11 lawsuits are virtually unknown and are replaced with merger objection claims. Many of these claims, though brought in high volume, are low impact, and the nominal fees to plaintiffs' counsel are a "tax" that all deal participants are willing to pay. However, if we view SPACs as vehicles for debuting firms to the public market that should disclose information of the same quality to their investors as is required in other IPOs, SPAC-related litigation currently appears unlikely to adequately fulfill this role. While government intervention could be an avenue to remedying any deficiencies in SPACs, reform of shareholder litigation—most urgently, pre-closing merger challenges—is necessary to help police future market innovations.

This Article proceeds as follows. Part I provides some brief background on SPACs and the litigation they have generated. Part II describes my data. Part III discusses descriptive statistics and empirical analysis, and Part IV investigates potential explanations for the odd inverse relationship between litigation probability with redemption rate. Part V compares merger liability in SPACs to section 11 liability in IPOs. Part VI assesses policy implications.

I. BACKGROUND

A special purpose acquisition company, or SPAC, is a public company formed by a sponsor that, following its IPO, has no operations except to search for a non-public firm to merge with and thereby bring public.[12] SPACs originated in the 1980s as "blank check" companies, which often made speculative investments and were considered penny stocks.[13] The SEC adopted tighter controls on blank check companies in 1990 with the Penny Stock Reform Act and Rule 419.[14] While SPACs have evolved in various ways (in some cases, specifically to avoid the strictures of Rule 419), many of their defining characteristics remain the same. In an IPO, SPACs typically sell units priced at $10. Most units consist of a share and a warrant entitling the holder to buy some percentage of a share for $11.50 at a date five years after the completion of the merger.[15] SPACs hold the proceeds from the IPO in an escrow account, in which they accumulate interest.[16] The sponsors of the SPAC have no access to the escrow account.[17] Sponsors usually retain 20% of the shares (called the "sponsor promote") as compensation, which are contingent on completing a merger.[18]

SPACs cannot form already having identified a merger target, and usually set an 18-to-24-month deadline to find and merge with a target company.[19] Once a target is identified, shareholders of the SPAC are informed and must vote to approve the merger. Independently however, shareholders must also decide whether to keep or redeem their shares; those who redeem are entitled to the price paid for the units, plus a pro rata share of any interest accrued in the trust.[20] Notably, shareholders who choose to redeem their shares can nonetheless both vote for the transaction and keep

12. Minmo Gahng, Jay R. Ritter & Donghang Zhang, SPACs 1 (July 13, 2022) (unpublished manuscript), https://ssrn.com/abstract=3775847 [https://perma.cc/XFX4-GQ3L].

13. *See* 17 C.F.R. § 230.419(a)(2)(ii) (2021).

14. William K. Sjostrom, Jr., *The Truth About Reverse Mergers*, 2 ENTREPRENEURIAL BUS. L.J. 743, 756–57 (2008) (describing blank check companies as "vehicles frequently used by boiler rooms in the 1980s for 'pump and dump' schemes").

15. Gahng et al., *supra* note 12.

16. The escrow funds are typically invested in short-term treasury bonds or qualifying money-market funds while the SPAC searches for a merger target. This feature has prompted recent arguments that SPACs are in fact illegal investment funds that should be registered under the Investment Company Act of 1940. *See Over 60 of the Nation's Leading Law Firms Respond to Investment Company Act Lawsuits Targeting the SPAC Industry*, ROPES & GRAY (Aug. 27, 2021), https://www.ropesgray.com/en/newsroom/alerts/2021/August/49-of-the-Nations-Leading-Law-Firms-Respond-to-Investment-Company-Act-Lawsuits [https://perma.cc/7G3L-WQU4].

17. Gahng et al., *supra* note 12.

18. *Id.* at 1–2.

19. *Id.* at 2.

20. *See id.*

their warrants (which are unbundled from the shares to trade separately following the IPO).[21] If, however, the SPAC managers fail to identify a merger target in the specified time period, the trust must be liquidated and paid out to shareholders, and sponsors receive nothing (although extensions of time are sometimes negotiated with shareholders).[22] Since it is not certain how many shareholders will choose to redeem their shares prior to the merger, de-SPAC transactions are negotiated to include a minimum amount of cash, and to meet this need, SPAC sponsors frequently arrange for private investment in public equity ("PIPE") funding.[23]

The popularity of the SPAC skyrocketed in 2020, raising as much cash in that year as in the entire preceding decade,[24] and the first quarter of 2021 alone saw more SPACs created and more money invested than in the entirety of 2020.[25] This meteoric rise has slowed since the second quarter of 2021,[26] although many previously formed SPACs are still shopping for merger partners, and new SPACs are continuing to form. The slowdown is likely the result not only of increased regulatory attention,[27] but of heightened overall scrutiny of SPAC performance.

A. ACCOUNTS OF THE 2020–2021 SPAC BOOM

Several expert accounts have painted damning portraits of the SPACs that are the product of the most recent bubble. Using a sample of all forty-seven SPACs that merged between January 2019 and June 2020, Michael Klausner, Michael Ohlrogge, and Emily Ruan found that the structure of SPACs creates substantial costs, misaligned incentives, and on the whole, losses for investors who own shares at the time of SPAC mergers (that is to say, those who do not redeem their shares). [28] These authors evaluated claims about the advantages SPACs offer over traditional IPOs: that they provide a

21. *Id.* at 1–2; *see also Redemption Rights at SPACs*, GREENBERG TRAURIG (June 28, 2021), https://www.gtlaw.com/en/insights/2021/6/published-articles/redemption-rights-bij-spacs [https://perma.cc/EG63-JB3L].

22. Gahng et al., *supra* note 12, at 2.

23. *Id.* Private investment in public entity ("PIPE") investors are generally private equity funds, hedge funds, and other accredited investors that buy a minority stake in a SPAC. Because one purpose of PIPE investment is to lock in a certain amount of capital in case of heavy redemptions, PIPE investors do not have redemption rights and generally receive their shares at a discount on the market price.

24. Klausner et al., *supra* note 4, at 230.

25. Bazerman & Patel, *supra* note 1.

26. *See, e.g.*, Alex Rankine, *The Stock Market's "Spac" Boom Is Slowing*, MONEYWEEK (July 16, 2021), https://moneyweek.com/investments/stockmarkets/603564/spac-boom-is-slowing [https://perma.cc/CAG4-R5AT]; Paul R. La Monica, *Welcome to the Big SPAC Slowdown*, CNN BUS. (Aug. 25, 2021), https://www.cnn.com/2021/08/25/investing/spacs-slowdown/index.html [https://perma.cc/R5SX-8AWR].

27. Rankine, *supra* note 26; La Monica, *supra* note 26.

28. Klausner et al., *supra* note 4, at 233–34.

less expensive, faster, and more certain route to the public markets; that they provide a path to being a public company that is often unavailable to firms engaged in complex or uncertain businesses that may be difficult to value; and that they provide more equal access to ordinary investors than alternatives such as private equity.[29] The authors found that SPACs fail on all fronts, largely because of the dilution built into the SPAC structure, and that SPACs tend to drop by at least one third of their value within a year of the merger.[30]

Minmo Gahng, Jay R. Ritter, and Donghang Zhang, in examining SPACs from 2010 to 2020, similarly found that SPAC returns tend to be negative, though cash-weighted returns are less so.[31] They also found that going public via a SPAC transaction is much more expensive for a private firm than undertaking a traditional IPO.[32] However, they found that sponsors take large haircuts and underwriters of SPACs surrender substantial commissions for weak deals, meaning when a SPAC experiences high redemption rates after announcing a merger.[33]

Finally, in a concise overview of the SPAC market as of the summer of 2021, Max H. Bazerman and Paresh Patel also suggested that the SPACs of 2020–2021 are not monolithic in type and have in fact been evolving over the course of the boom. The authors suggested that although not all SPACs are successful, they offer financing opportunities "that compete with later-stage venture capital, private equity, direct listings, and the traditional IPO process [and provide] an infusion of capital to a broader universe of start-ups and other companies, fueling innovation and growth."[34] They noted that although SPACs had a "questionable start" as blank check companies and have existed as a "niche" "cottage industry" for most of the intervening years, the format has gone mainstream.[35]

B. THE SPAC LITIGATION DELUGE

The structure of a SPAC lends itself to various critiques, and thus, legal claims. De-SPAC transactions occur, by definition, under significant time pressure. Moreover, neither the management (via the sponsor promote) nor the underwriter (via commissions) of the SPAC are compensated at all unless a transaction actually occurs. This setup creates incentives for sponsors to

29. *Id.* at 230–35.
30. *See id.*
31. *See* Gahng et al., *supra* note 12, at 4.
32. *Id.* at 6.
33. *Id.* at 6–7.
34. Bazerman & Patel, *supra* note 1, at 104.
35. *Id.* at 105.

close a transaction—perhaps any transaction—rather than liquidate the trust. Additionally, the twenty-four-month time limit means that the SPAC may lack the means or opportunity to conduct sufficient diligence on the target or adequately evaluate the full universe of merger options. Moreover, as the end of the time limit approaches, targets may have increased leverage in negotiations with the SPAC, and though it may serve the sponsors and managers to close the deal before the deadline, shareholders might be better served by extending the deadline or waiting for a more attractive deal.[36] PIPE financing may give rise to additional conflicts of interest by allowing a merger to close at the cost of substantial dilution for the original SPAC shareholders.[37]

Failure to disclose these conflicts could lead to lawsuits under the securities laws.[38] Moreover, SPACs are vulnerable to lawsuits alleging that sponsors breached their fiduciary duties in pursuing the merger, and they may face greater judicial scrutiny of these claims because the SPAC directors may not be disinterested.[39] The de-SPAC transaction may be subject to lawsuits both before and after the merger under Rule 14a-9, which governs the content of proxy disclosures. Broadly, SPACs (and their targets, once the transaction closes) are also public companies and therefore subject to the reporting requirements and fraud prohibitions of the federal securities laws, and thus, false statements and inadequate periodic disclosures may give rise to liability.[40]

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36. *See* Press Release, Paul Munter, Acting Chief Acct., U.S. Sec. & Exch. Comm'n, Financial Reporting and Auditing Considerations of Companies Merging with SPACs (Mar. 31, 2021), https://www.sec.gov/news/public-statement/munter-spac-20200331 [https://perma.cc/ZUK8-54H3]; Press Release, U.S. Sec & Exch. Comm'n Div. Corp. Fin., Staff Statement on Select Issues Pertaining to Special Purpose Acquisition Companies (Mar. 31, 2021), https://www.sec.gov/news/public-statement/division-cf-spac-2021-03-31 [https://perma.cc/23SP-KP5N]; Caitlyn M. Campbell, *Surge in SPACtivity Leads to Litigation and Regulatory Risks*, NAT'L L. REV. (Apr. 5, 2021), https://www.natlawreview.com/article/surge-spactivity-leads-to-litigation-and-regulatory-risks [https://perma.cc/9749-YA6H].

37. *See* Campbell, *supra* note 36.

38. *Id.*

39. *See* Michael Klausner & Michael Ohlrogge, *SPAC Governance: In Need of Judicial Review* 3 (N.Y.U. Working Paper No. 22-07, 2021), https://ssrn.com/abstract=3967693 [https://perma.cc/TX83-67Y7]; *see also In re* MultiPlan Corp. Stockholders Litigation, 268 A.3d 784, 784–85 (Del. Ch. 2022); Christopher Kercher, Ellison Ward Merkel, Andrew Rossman & R. Brian Tommons, *Litigation Risk in the SPAC World*, JDSUPRA (Oct. 1, 2021), https://www.jdsupra.com/legalnews/litigation-risk-in-the-spac-world-88058 [https://perma.cc/EFF3-P8EE] (noting that the business judgment rule is unlikely to apply, and the duties of SPAC management in de-SPAC transactions are likely to be reviewed under an "entire fairness" standard).

40. Rodrigues & Stegemoller, *supra* note 4, at 46.

Practitioner reports raising alarm about rising SPAC-related litigation began in earnest in spring 2021.[41] This coincided with multiple announcements that the SEC would scrutinize SPACs more closely.[42] Various journalists and industry participants have reported informal tallies,[43] but there has so far been no deep dive into the characteristics and drivers of these lawsuits. In the recent surge of SPAC litigation, which claims predominate, and why? What are the characteristics of de-SPAC transactions that generate lawsuits versus those that do not? Who are the plaintiffs and firms bringing these lawsuits? More importantly, does this surge in litigation reflect SPAC quality, and does it offer a remedy to any of the potential negative outcomes arising from the controversial features of the SPAC format? This Article makes a first attempt at answering these questions.

II. DATA

To assess the recent increase in SPAC litigation, I compose two samples: a sample of lawsuits and a sample of transactions. For my sample of lawsuits, I search Bloomberg Law for dockets in federal district courts, Delaware Chancery Court, and New York Supreme Court[44] containing any references to special purpose acquisition companies. I then manually screen the complaints and dockets of these lawsuits to determine whether the

41. *See, e.g.*, *id.*; Campbell, *supra* note 36; Glenn A. Kopp, Jason Linder, Glenn K. Vanzura & Bradley A. Cohen, *Mitigating SPAC Enforcement and Litigation Risks*, MAYER BROWN (Apr. 26, 2021), https://www.mayerbrown.com/en/perspectives-events/publications/2021/04/mitigating-spac-enforcement-and-litigation-risks [https://perma.cc/S8YR-2AMR]; Edvard Pettersson & Crystal Tse, *Liability for SPAC Flops: Waitr Could Be Test Case for Disgruntled Investor Lawsuits*, INS. J. (Feb. 16, 2021), https://www.insurancejournal.com/news/national/2021/02/16/601362.htm [https://perma.cc/3ELD- D8A4]; Rappaport et al., *supra* note 6; Todd, *supra* note 6; Client Memorandum from Paul Weiss, The SPAC Litig. Boom: What SPAC Sponsors, Dirs. & Officers Can Do to Mitigate Their Exposure (Mar. 9, 2021), https://www.paulweiss.com/media/3980884/the_spac_litigation_boom_what_spac_sponsors_directors_and_officers_can_do_to_mitigate_their_exposure.pdf [https://perma.cc/5DFB-2A57]; Varant Yegparian & Schiffer Hicks Johnson, *How to Prepare for the Deluge of SPAC Litigation*, JDSUPRA (Apr. 22, 2021), https://www.jdsupra.com/legalnews/how-to-prepare-for-the-deluge-of-spac-2261276 [https://perma.cc/76GY-BNPW]; *SPAC Litigation and Enforcement Update*, BAKER BOTTS (Apr. 23, 2021), https://www.bakerbotts.com/thought-leadership/publications/2021/april/spac-litigation-and-enforcement-update-spring-2021 [https://perma.cc/7K2G-QH2Q]; Jeffrey I. Lang & Luke Appling, *The Growth of SPAC-Related Litigation*, COHEN & GRESSER (May 27, 2021), https://www.cohengresser.com/app/uploads/2021/05/The-Growth-of-SPAC-Related-Litigation.pdf [https://perma.cc/A2SU-BRB9].

42. *See, e.g.*, Press Release by Paul Munter, *supra* note 36; Press Release by Sec. & Exch. Comm'n. Div. Corp. Fin., *supra* note 36.

43. *See* Frankel, *supra* note 7; LaCroix, *supra* note 7; Leo Cho, *SPAC Related Filings on the Rise*, STAN. L. SCH. SEC. CLASS ACTION CLEARINGHOUSE (June 7, 2021), https://securities.stanford.edu/news-reports/20210607-SPAC-Related-Filings-on-the-Rise.pdf [https://perma.cc/A2U5-4LD8] (reporting an increase in SPAC-related litigation as a percentage of securities class actions).

44. I include this jurisdiction following press reports of an explosion in SPAC-related litigation in New York Supreme Courts. *See* Frankel, *supra* note 7; Rappaport et al., *supra* note 6.

lawsuit arises from a de-SPAC transaction,[45] and if so, what claims are brought.[46] I also gather information on plaintiff law firms and outcomes (if any) from these dockets. My search extends from January 1, 2017, to June 30, 2021.

Next, I compose a sample of all SPAC transactions from January 1, 2014, to July 31, 2021, from SPACInsider and the SEC EDGAR website. I use this range to account for several factors. First, although most claims in my sample are securities claims that have relatively short limitations periods, there are a non-trivial number of contract claims whose statute of limitations is significantly longer. However, my 2017 docket search captured very few lawsuits involving SPACs, and only one involved a transaction that occurred before 2014. I include lawsuits that were filed before June 30, 2021, but many of the cases in my sample are merger objection cases that are filed before the closing of the transaction; accordingly, I extend my transaction sample an additional month. The SPACInsider database furnishes redemption rate, IPO proceeds, implied enterprise value, and warrants issued in the IPO for the majority of these transactions (for those that are omitted, I use SEC EDGAR). I search the websites of the target firm for each transaction to find the target's age at the time of the de-SPAC. To assess the quality of the sponsors, I code the number of SPACs each management team has participated in at the time of the de-SPAC transaction, which I source from SPACInsider or internet searches.[47] Finally, I take data on returns and dividends for all merged companies from Compustat Daily.[48]

III. DESCRIPTIVE STATISTICS AND EMPIRICAL ANALYSIS

In this Part, I first compare the characteristics of de-SPAC transactions that generated lawsuits to those that did not. I then examine the attributes of the lawsuits in my sample. Finally, I examine the associations between lawsuits and various transaction characteristics.

45. I omit, for instance, bankruptcy cases and lawsuits brought by potential SPAC targets where the SPAC ultimately selected a different target.

46. I omit from my coding all control person claims, which are almost universally brought with any claims under the federal securities laws.

47. In unreported specifications, I also use alternative measures of sponsor quality (or at least, notoriety) by following in the spirit of Klausner, Ohlrogge, and Ruan. *See* Klausner et al., *supra* note 4, at 251–52. Accordingly, I code whether the manager or owner of the sponsor was previously a high-level manager or founder of a U.S. or Global Fortune 500 company or a company commonly considered a household name (for example, MGM Resorts, Allergan, and Virgin Media) that previously appeared in the Fortune 500. I also code whether the sponsor is affiliated with a fund with more than $1 billion in assets under management. *Id.*

48. Pricing data downloaded August 21, 2021.

A. COMPARING TRANSACTIONS THAT GENERATED LAWSUITS TO THOSE THAT DID NOT

De-SPAC transactions that are subject to at least one lawsuit differ along a few key dimensions from those that are not. These descriptive statistics are reported in Table 1. First, the redemption rates of the transactions that generated lawsuits are significantly lower. The average percentage of shareholders that opted to redeem their shares in de-SPAC transactions that generated lawsuits is roughly 21%; the rate is more than double in de-SPAC transactions that generated no lawsuits at nearly 45%. Perhaps unsurprisingly, the de-SPAC transactions generating lawsuits have significantly higher implied enterprise values: roughly $2.15 billion as opposed to roughly $1.4 billion for de-SPAC transactions that did not draw lawsuits. Transactions generating lawsuits also originated from SPAC IPOs with higher proceeds than those which did not generate lawsuits, with averages of roughly $369 million and $256 million, respectively. Transactions generating lawsuits offer a smaller percentage of a warrant (that can later be used to purchase a share) with each unit sold in the IPO: sued transactions offer an average of 0.44 warrants per unit, as opposed to unsued transactions, which offer an average of nearly 0.55 warrants per unit. Consistent with industry commentary, the age of the target firm is lower for de-SPAC transactions that generate lawsuits with an average of twelve years versus nearly forty-three. However, the median target firm ages are nine and ten years, respectively, and therefore this difference is not significant.[49] Finally, de-SPAC transactions generating lawsuits take about one month longer on average to complete, at 22.4 versus 21.36 months. Although I compare and report the average three-day, seven-day, fourteen-day, thirty-day, and ninety-day post-merger returns for de-SPAC transactions that were sued versus those that were not, there is no statistically significant difference.

49. I note that firm age is also largely (though not entirely) likely to track whether the firm is pre-revenue, which may also indicate a riskier target.

TABLE 1. Characteristics of Sued and Unsued De-SPAC Transactions

	Sample of Sued De-SPACs				*Sample of Unsued De-SPACs*				
	Mean	*Median*	*Standard Deviation*	*Obs.*	*Mean*	*Median*	*Standard Deviation*	*Obs.*	*t-stat*
Redemption Rate (%)	21.41995	.4683396	31.41641	62	44.83333	50.95	38.0758	168	4.3270
Implied Enterprise Value ($m)	2150.54	1283.5	2739.276	62	1399.343	925	1814.378	165	-2.3949
IPO Proceeds ($m)	369.3452	250	347.367	62	255.9107	229.5	178.7456	168	-3.2349
Warrants	.4442623	.5	.2057031	61	.5477912	.5	.2635458	166	2.7721
Target age at SH vote (years)	12.09677	9	11.54849	62	42.92216	10	218.1146	167	1.1107
Months to complete	22.40323	24	2.58913	62	21.3631	24	3.745537	168	-2.0148
3-day returns	-.0467387	-.0716895	.1475693	28	-.0051028	-.0234741	.1691097	81	1.1585
7-day returns	-.049506	-.1012345	.2070382	53	-.0304111	-.054142	.3861426	142	0.3418
14-day returns	-.0338234	-.0839047	.2580448	54	-.0118041	-.0599034	.653251	141	0.2403
30-day returns	-.0358618	-.1304813	.3650061	29	-.0495576	-.0575954	.2386171	77	-0.2258
90-day returns	-.0484598	-.1514094	.4531122	36	-.0102963	-.0514618	.4307399	84	0.4379

Notes: The sample of sued transactions includes all lawsuits involving a de-SPAC transaction filed between January 1, 2017, and June 30, 2021, located on a Bloomberg Law search of all federal, Delaware Chancery, and New York Supreme Court dockets. The full sample includes all de-SPAC transactions completed between January 1, 2014, and July 31, 2021, sourced from SPACInsider.

In Table 2, I report the most common industries represented among the target firms of sued and unsued de-SPAC transactions, based on Fama-French 48 industry classification. The business services industry supplies the target firms for many de-SPAC transactions that are sued and many that are not: 26.67% and 24.85% respectively. While 13.3% of the target firms in sued transactions come from the automotive industry, only 5.45% of the target firms that do not generate lawsuits are in this industry. Similarly, a higher percentage of target firms that draw lawsuits are involved in electrical equipment (8.33%) than those that do not (1.82%). Conversely, transactions involving petroleum and natural gas targets comprise 4.85% of the unsued transactions, but none of the transactions generating lawsuits. While 10.3% of unsued transactions involve pharmaceutical targets, only 3.3% of the sued transactions do. It is interesting to note that across almost all industries reported in this table, redemption rates are higher, sometimes significantly, for the transactions that are not sued than for those that are (the exception is the electrical equipment industry, which furnished just 1.82% of the target firms for unsued de-SPAC transactions).

TABLE 2. Industries of Target Firms in Sued and Unsued De-SPAC Transactions Based on Fama-French 48 Classification

	Sample of Sued De-SPAC Transactions						*Sample of Unsued De-SPAC Transactions*					
Industry	*Freq.*	*%*	*Mean Redem. Rate*	*Mean Ent. Value*	*Mean IPO Proc.*	*Mean Target Age*	*Freq.*	*%*	*Mean Redem Rate*	*Mean Ent. Value*	*Mean IPO Proc.*	*Mean Target Age*
Pharmaceutical Products	2	3.33	7	405	93	3	17	10.30	50	615	124	7
Business Services	16	26.67	36	2571	463	14	41	24.85	43	1832	324	69
Automobiles and Trucks	8	13.33	4	2820	512	7	9	5.45	18	2161	258	29
Retail	4	6.67	16	1213	278	19	7	4.24	71	507	131	15
Petroleum and Natural Gas	0	0					8	4.85	32	955	312	7
Entertainment	3	5	52	760	149	4	6	3.64	53	1137	266	15
Electrical Equipment	5	8.33	41	1291	294	26	3	1.82	20	964	185	18.3
Banking	3	5	27	2689	397	9	6	3.64	43	3367	241	15
Other	19	31.67					68	41.2				

Notes: This table includes only industries that comprise roughly 5% or more of the target firms in either sample.

B. INCIDENCE AND ATTRIBUTES OF SPAC-RELATED LAWSUITS

In Tables 3, 4 and 5, I report the incidence and characteristics of the lawsuits in my sample. Table 3 reports lawsuits by claim, court, and year. The most prominent observation is the dearth of SPAC-related lawsuits in 2017, 2018 and 2019, the dramatic rise from 2019 to 2020 (from nine lawsuits to forty-six), and the near-doubling of that number in the first half of 2021 alone (to eighty-nine).[50] Lawsuits filed in federal and New York

50. I count each separately filed complaint as a lawsuit, even though some are eventually consolidated. However, I do not count twice lawsuits that are simply transferred to other jurisdictions.

Supreme Courts are largely responsible for this spike (although Delaware has seen a surprising rise—from zero to thirteen lawsuits—in the first half of 2021). The rise in lawsuits generally corresponds with the increase in total SPAC transactions, although the lawsuit curve is shorter and steeper in 2020 and 2021. Notably, the increase in lawsuits corresponds with a sizable decrease in the average redemption rate for all de-SPAC transactions in 2020 and the first half of 2021.

I further tabulate the claims for each lawsuit (I note here that many lawsuits have more than one claim). I report only the most common claims, which are Rule 10b-5 claims, Rule 14a-9[51] claims, state law claims for breach of fiduciary duty, and contract claims.[52] The most dramatic jump has been in claims brought under state fiduciary law in 2020 and 2021, followed by Rule 10b-5 claims. Rule 14a-9 claims experienced a less pronounced jump, and contract claims have remained low and relatively stable over all the years of the sample. section 11 claims have predictably been virtually nonexistent.

TABLE 3. Lawsuits for Sued Transactions by Main Claim Types (January 1, 2017–June 30, 2021)

Year	*10b5 Claims*	*Sec. 11 Claims*	*14a Claims*	*State Fid. Duty Claims*	*Contract Claims*	*Total Lawsuits*	*Federal Court*	*Del. Ch. Court*	*NY Sup. Court*	*Total de-SPACs*	*Mean Redem. Rate of Total de-SPACs (%)*
2017	1	0	0	1	2	4	1	1	2	13	47.39
2018	0	0	0	0	1	2	1	1	0	22	54.05
2019	5	2	8	0	0	9	9	0	0	28	64.96
2020	9	0	11	30	8	46	21	0	25	64	37.45
2021 (as of June 30)	38	1	18	42	4	89	56	13	20	85*	22.98
Total	53	3	37	73	15	150	88	15	47	212	

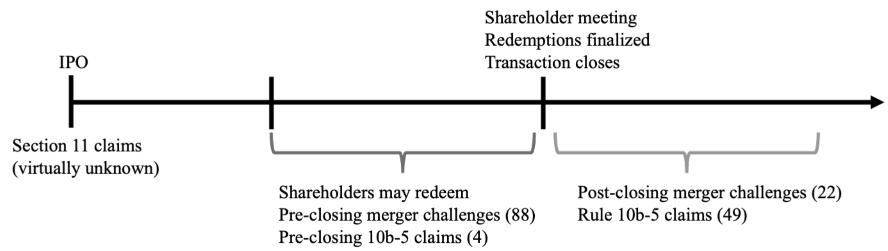
Notes: Each individual lawsuit may have more than one main claim type. All are tabulated here. Less common claim types, such as unjust enrichment and corporate waste, have been omitted from this table.
*Reports transactions closed as of July 31, 2021

51. 17 C.F.R. § 240.14a-9. For simplicity, this Article will refer to this Rule as simply "Rule 14a-9").

52. For comparative purposes, I also report claims under section 11 of the Securities Act ("section 11"). I omit less common claims from this tabulation, such as unjust enrichment, waste, and common law fraud. I also do not report control person liability claims, which are almost universally brought along with any claim under the federal securities laws.

Figure 1 illustrates the timing of these claims. Eighty percent (88) of the claims brought under Rule 14a-9 and state fiduciary duties are brought *before* the de-SPAC merger, meaning that these claims seek injunctions.[53] The remaining 20% (22) of these claims are brought after the merger for damages. Conversely, 92% (49) of the Rule 10b-5 claims in my sample are brought after the merger.

FIGURE 1. SPAC Litigation Timeline



I also report in Table 4 the transaction characteristics associated with each type of claim. Transactions associated with contract claims have by far the highest average redemption rate at 35.44%, the lowest average SPAC IPO proceeds at $247.87 million, and take the longest to complete at 23.4 months. Redemption rates for other claim types range from 13.44% to 18.73%, and IPO proceeds from $384.68 million to $412.18 million. Transactions targeted with contract and state fiduciary claims are associated with the highest implied enterprise values, at $2.612 billion and $2.521 billion; Rule 14(a) and Rule 10b-5 claims target transactions with median $2.146 billion and $2.048 billion respectively. Warrants range between 0.4 and 0.49 per unit, and average target age from 9.55 to 13 years.

53. Generally, these complaints also purport to seek damages in the event that the transaction is consummated.

TABLE 4. Transaction Characteristics by Claim Type

	10b5			*14a*			*State Fiduciary Duty*			*Contract*		
	Mean	*Med.*	*Obs.*	*Mean*	*Med.*	*Obs.*	*Mean*	*Med.*	*Obs.*	*Mean*	*Med.*	*Obs.*
Redemption Rate (%)	14.5	.1	20	18.732	.1	25	13.44197	.1	39	35.44367	24.11834	10
Implied Enterprise Value ($m)	2048.775	1046.5	20	2146.336	1267	25	2521.595	1570	39	2612.36	1504	10
IPO Proceeds ($m)	412.18	236.9	20	402.452	280	25	384.6821	280	39	247.87	230	10
Warrants	.4710526	.5	19	.49	.5	25	.3970085	.333	39	.4	.5	10
Target age at SH vote (years)	9.55	7.5	20	10.6	5	25	13	10	39	12.9	9	10
Months to complete	21.75	24	20	22.8	24	25	22.69231	24	39	23.4	24	10

Finally, in Table 5, I tabulate the plaintiff law firms associated with the total number of lawsuits, as well as with each type of claim. I classify plaintiff firms as top plaintiff firms, entrepreneurial SPAC firms, entrepreneurial emerging firms, and top defense firms. Top plaintiff firms are those that appear on the Legal 500 list for securities plaintiff litigation.[54] These are Berman Tobacco, Bernstein Litowitz, Grant & Eisenhofer, Labaton Sucharow, Pomerantz, Quinn Emmanuel, and Robbins Geller. Entrepreneurial SPAC firms are those that brought 5% or more of the lawsuits in my sample. These are Brodsky & Smith, Monteverde & Associates, Moore Kuehn, Pomerantz, Rigrodsky Law, and Robbins Geller. Entrepreneurial emerging firms in my sample are those identified by Klausner and Heglund.[55] The emerging entrepreneurial firms in my sample are Glancy Prongay & Murray, Kahn Swick & Foti, and the Rosen Law Firm. Finally, top defense firms in my sample are King & Spaulding, McDermott Will & Emery, and Williams & Connolly.

The entrepreneurial SPAC firms lead the pack, with more than twice as many lawsuits as any other category. Notably, the primary main claims

54. *Securities Litigation: Plaintiff*, LEGAL 500 (2022), https://www.legal500.com/c/united-states/dispute-resolution/securities-litigation-plaintiff [https://perma.cc/KR7X-RU39].

55. Guest Post by Michael Klausner & Jason Hegland, *Guest Post: Deeper Trends in Securities Class Actions 2006–2015*, D&O DIARY (June 23, 2016), https://www.dandodiary.com/2016/06/articles/securities-litigation/guest-post-deeper-trends-in-securities-class-actions-2006-2015 [https://perma.cc/U5H7-KLY4]. I note that their list includes Pomerantz, which I omit because it has appeared for the last two years in the Legal 500.

driving this result are Rule 14a-9 proxy fraud claims at twenty-one and, even more pronounced, claims under state fiduciary law at fifty-three (hereinafter I refer to these collectively as "merger objection claims"). Rule 10b-5 claims are relatively stable across the three categories of traditional plaintiff firms, with nineteen by top plaintiff firms, sixteen by entrepreneurial SPAC firms, and thirteen by other entrepreneurial emerging firms. The firms traditionally serving defendants, by contrast, are almost exclusively involved in SPAC-related lawsuits by virtue of contract claims, which form a small minority of the main claim types that I tabulate. These claims typically involve disputes among management, or between sponsors/management and PIPE investors, which likely accounts for the involvement of non-plaintiff firms.

TABLE 5. Lawsuits by Firm

	Total Lawsuits	*10b5*	*14a*	*State Fiduciary Duty*	*Contract*
Top Plaintiff Firms	27	19	4	4	1
Entrepreneurial SPAC Firms	82	23	23	55	0
Entrepreneurial Emerging Firms	14	13	4	3	0
Top Defense Firms	7	0	0	1	5

C. EMPIRICAL ANALYSIS

Table 6 shows the results of OLS regressions in which the dependent variable is a dummy equal to one if the de-SPAC transaction generates at least one lawsuit, and the independent variable is redemption rate. I control throughout for industry using a dummy variable equal to one if the target firm of the de-SPAC transaction is in an industry found by other studies to be particularly vulnerable to securities litigation, including the biotechnology, computer hardware, electronics, retail, or computer software industries.[56] I also control for the log of implied enterprise value of the transaction to assess whether lawsuits are driven by the estimated value of the deal. I control for the target age in years to test anecdotal claims that plaintiff lawyers target de-SPAC transactions involving younger firms. I also control for several proxies for the quality of the de-SPAC merger, including

56. *See* Douglas J. Skinner, *Earnings Disclosures and Stockholder Lawsuits*, 23 J. ACCT. & ECON. 249, 256 n.5 (1997); Jonathan L. Rogers & Phillip C. Stocken, *Credibility of Management Forecasts*, 80 ACCT. REV. 1233, 1257 (2005); Francois Brochet & Suraj Srinivasan, *Accountability of Independent Directors: Evidence from Firms Subject to Securities Litigation*, 111 J. FIN ECON. 430, 448 (2014).

the log of the IPO proceeds of each transaction[57] and the number of warrants per unit issued in the IPO.[58] Finally, I use the number of SPAC transactions the management team had completed prior to the closing of the transaction as a proxy for quality of the management team.[59] All regressions include robust standard errors. To control for the possibility that plaintiffs simply brought more lawsuits at the same time due to some unobserved trend, all regressions include year fixed effects.

The coefficient on redemption rate is negative and statistically significant in all specifications. The coefficient on redemption rate is relatively stable across specifications and is significant at the 5% level in the final specification which includes the most controls (it is significant at the 1% level in several other specifications). The likelihood of a lawsuit rises roughly 0.26% for every 1% decrease in redemption rate. In other words, a de-SPAC transaction with a 25% redemption rate is 13% more likely to generate at least one lawsuit than a transaction in which 75% of the shareholders redeem their shares in advance of the merger.

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57. *See id.*; *see also* Klausner et al., *supra* note 4, at 240 (using IPO proceeds in alternative specifications as a measure for SPAC quality).

58. Bazerman & Patel, *supra* note 1, at 106 (characterizing SPACs that "raised relatively small amounts of capital and offered higher-than-average warrants as an incentive to entice investors" as "indications of lower-quality sponsor teams"). I note in addition that the warrants per share may impact redemption rate; the reason is that if shareholders retain less upside without their shares, they may be less likely to redeem. The pairwise correlation between redemption rate and warrants is 0.31. In any case, I control for both variables, thereby addressing concerns that the redemption variable may be capturing the warrants per share.

59. As an alternate measure of sponsor quality, in unreported specifications I use a dummy equal to one if the sponsor owner or manager was the owner or manager of a well-known company and a dummy equal to one if the sponsor was affiliated with a fund with over $1 billion in assets under management. The coefficient on redemption rate is similar and also significant at the 5% level.

TABLE 6. Probability of a Lawsuit

	(1)	(2)	(3)	(4)	(5)	(6)
	Lawsuit Dummy	*Lawsuit Dummy*	*Lawsuit Dummy*	*Lawsuit Dummy*	*Lawsuit Dummy*	*Lawsuit Dummy*
Redemption Rate	-0.00309***	-0.00270**	-0.00281**	-0.00277**	-0.00262**	-0.00262**
	(-4.05)	(-3.18)	(-3.30)	(-3.23)	(-3.01)	(-3.00)
Vulnerable Industry Dummy	0.0153	0.0414	0.0472	0.0472	0.0553	0.0575
	(0.25)	(0.64)	(0.73)	(0.73)	(0.84)	(0.86)
Log Enterprise Value ($m)		0.0431	0.0465	0.0312	0.0259	0.0274
		(1.45)	(1.56)	(0.75)	(0.61)	(0.63)
Target Age (years)			-0.000277**	-0.000257*	-0.000222	-0.000222
			(-2.68)	(-2.24)	(-1.92)	(-1.91)
Log IPO Proceeds				0.0298	0.0313	0.0338
				(0.51)	(0.51)	(0.55)
Warrants					-0.138	-0.142
					(-1.14)	(-1.17)
Repeat Player						-0.00703
						(-0.29)
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
_cons	0.211**	-0.657	-0.714	-0.956	-0.784	-0.850
	(3.01)	(-1.08)	(-1.17)	(-1.23)	(-0.89)	(-0.94)
r2_a	0.0658	0.0714	0.0758	0.0724	0.0750	0.0710
N	230	227	226	226	223	223

Notes: *T* statistics in parentheses - * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$.

I then bifurcate the sample based on claim type. Table 7 shows the results of OLS regressions in which the dependent variable is a dummy equal to one if the de-SPAC transaction generates at least one merger objection claim (either a state fiduciary duty claim or a Rule 14a-9 claim) after dropping transactions that generate lawsuits but no merger objection claims.

Table 8 shows the results of OLS regressions in which the dependent variable is a dummy equal to one if the de-SPAC transaction generated at least one claim under Rule 10b-5 after dropping transactions that generate lawsuits but no Rule 10b-5 claims. I use identical controls as in Table 6,[60]

60. Vulnerable Industries Dummy equals one if the merged firm belongs to the biotechnology, computer hardware, electronics, retail, or computer software industries. These industries have been found

and all regressions include year fixed effects. Although the samples are small, the coefficients on redemption rate are very similar to the one I find in Table 6. A 1% increase in redemption rate corresponds with a 0.25% decrease in the likelihood of a merger objection claim and a 0.22% decrease in the likelihood of a Rule 10b-5 claim.

TABLE 7. Probability of a Merger Objection Claim

	(1)	(2)	(3)	(4)	(5)	(6)
	Merger Objection Dummy	*Merger Objection Dummy*	*Merger Objection Dummy*	*Merger Objection Dummy*	*Merger Objection Dummy*	*Merger Objection Dummy*
Redemption Rate	-0.00294***	-0.00267**	-0.00275***	-0.00266**	-0.00254**	-0.00254**
	(-4.07)	(-3.31)	(-3.38)	(-3.24)	(-3.08)	(-3.06)
Vulnerable Industry Dummy	-0.0458	-0.0244	-0.0199	-0.0199	-0.0122	-0.0122
	(-0.80)	(-0.40)	(-0.33)	(-0.33)	(-0.20)	(-0.19)
Log Enterprise Value ($m)		0.0312	0.0343	0.00555	0.00668	0.00670
		(1.09)	(1.19)	(0.14)	(0.16)	(0.16)
Target Age (years)			-0.000200*	-0.000159	-0.000144	-0.000144
			(-2.45)	(-1.69)	(-1.51)	(-1.51)
Log IPO Proceeds				0.0581	0.0499	0.0500
				(1.02)	(0.84)	(0.84)
Warrants					-0.103	-0.104
					(-0.87)	(-0.87)
Repeat Player						-0.0000783
						(-0.00)
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
_cons	0.213**	-0.415	-0.468	-0.967	-0.769	-0.769
	(3.07)	(-0.71)	(-0.79)	(-1.29)	(-0.88)	(-0.87)
r2_a	0.0952	0.0965	0.0992	0.0990	0.101	0.0963
N	215	212	211	211	209	209

Notes: *T* statistics in parentheses - * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$.

by previous studies to be particularly vulnerable to securities litigation. *See* Skinner, *supra* note 56; Rogers & Stocken, *supra* note 56; Brochet & Srinivasan, *supra* note 56. Repeat Player is the number of SPAC transactions in which the management team previously participated. All regressions include robust standard errors and year fixed effects.

TABLE 8. Probability of a Rule 10b-5 Claim

	(1)	*(2)*	*(3)*	*(4)*	*(5)*	*(6)*
	10b-5 Dummy	*10b-5 Dummy*	*10b-5 Dummy*	*10b-5 Dummy*	*10b-5 Dummy*	*10b-5 Dummy*
Redemption Rate	-0.00237^{***}	-0.00223^{***}	-0.00231^{***}	-0.00232^{***}	-0.00218^{**}	-0.00221^{**}
	(-3.74)	(-3.42)	(-3.48)	(-3.49)	(-3.21)	(-3.22)
Vulnerable Industry Dummy	-0.0277	-0.0134	-0.00745	-0.00756	-0.00170	0.00214
	(-0.64)	(-0.30)	(-0.16)	(-0.17)	(-0.04)	(0.04)
Log Enterprise Value ($m)		0.0166	0.0188	0.0263	0.0252	0.0287
		(0.77)	(0.86)	(0.97)	(0.91)	(1.03)
Target Age (years)			-0.000181^{*}	-0.000190^{*}	-0.000167^{*}	-0.000167^{*}
			(-2.48)	(-2.41)	(-2.19)	(-2.19)
Log IPO Proceeds				-0.0141	-0.00571	-0.00207
				(-0.27)	(-0.11)	(-0.04)
Warrants					-0.0531	-0.0629
					(-0.52)	(-0.62)
Repeat Player						-0.0150
						(-1.25)
Year Fixed Effects	Yes	Yes	Yes	Yes	Yes	Yes
_cons	0.170^{**}	-0.165	-0.201	-0.0896	-0.190	-0.306
	(2.88)	(-0.38)	(-0.46)	(-0.13)	(-0.23)	(-0.37)
r2_a	0.0956	0.0952	0.0974	0.0926	0.0867	0.0851
N	188	185	184	184	181	181

Notes: *T* statistics in parentheses - $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$.

In Table 9, I drop de-SPAC transactions that generated no lawsuits and regress the number of lawsuits per transaction on redemption rate, including the same controls. There is no statistically significant association between the number of lawsuits and redemption rate, although interestingly, the number of lawsuits is negatively related to the vulnerable industry dummy at the 10% significance level in every specification. Less surprisingly, the number of lawsuits per transaction is positively related to the log of the implied enterprise value of the merger at the 10% significance level in the specification including all controls. It seems, accordingly, that while the likelihood of being sued at all is unrelated to deal size, in the subset of transactions that draw at least one lawsuit, large deals draw more litigation than small deals. I note, however, that the number of observations is small, and therefore the predictive power of these regressions may be limited.

TABLE 9. Number of Lawsuits in Sued De-SPAC Transactions

	(1)	*(2)*	*(3)*	*(4)*	*(5)*	*(6)*
	Lawsuits	*Lawsuits*	*Lawsuits*	*Lawsuits*	*Lawsuits*	*Lawsuits*
Redemption Rate	-0.00740	-0.00256	-0.00156	-0.00190	-0.00162	-0.00146
	(-1.18)	(-0.42)	(-0.29)	(-0.35)	(-0.31)	(-0.29)
Vulnerable Industry Dummy	-0.905*	-0.894*	-0.858*	-0.849*	-0.862*	-0.823*
	(-2.34)	(-2.50)	(-2.40)	(-2.33)	(-2.33)	(-2.32)
Log EnterpriseValue ($m)		0.525**	0.578***	0.626*	0.648*	0.675**
		(3.28)	(3.76)	(2.49)	(2.66)	(2.75)
Target Age (years)			-0.0132	-0.0117	-0.0127	-0.0143
			(-0.64)	(-0.47)	(-0.47)	(-0.51)
Log IPO Proceeds				-0.100	-0.210	-0.128
				(-0.21)	(-0.42)	(-0.25)
Warrants					-0.590	-0.710
					(-0.64)	(-0.72)
Repeat Player						-0.109
						(-0.83)
_cons	2.788***	-8.318*	-9.301**	-8.370	-6.413	-8.418
	(7.55)	(-2.47)	(-2.96)	(-1.42)	(-1.02)	(-1.22)
r2_a	0.0485	0.123	0.113	0.0982	0.0792	0.0693
N	62	62	62	62	61	61

Notes: *T* statistics in parentheses - * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$

In Table 10, I regress three, seven, fourteen, thirty, and ninety-day returns for the merged firms in my sample on number of lawsuits, controlling for the age of the target firm to assess whether there is a relationship between number of lawsuits and the ultimate success of the merger.[61] There is no statistically significant association in any specification. Finally, to assess whether the likelihood of a 10b-5 lawsuit is related to returns on the merger,

61. I also collect one-year and three-year returns, but my sample yields insufficient observations for these timeframes.

in unreported results, I regress a dummy equal to one if the transaction generated a 10b-5 claim on three, seven, fourteen, thirty, and ninety-day returns, controlling for firm age. There is no statistically significant association with returns in any specification.[62]

TABLE 10. Returns

	(1)	*(2)*	*(3)*	*(4)*	*(5)*
	Day 3 Returns	*Day 7 Returns*	*Day 14 Returns*	*Day 30 Returns*	*Day 90 Returns*
Total Lawsuits	-0.0117	0.00131	0.0176	0.0110	-0.0109
	(-1.18)	(0.10)	(1.12)	(0.47)	(-0.43)
Target Age (years)	0.00000827	0.0000567*	0.0000455*	0.000174	0.0000264
	(0.69)	(2.21)	(2.28)	(0.21)	(0.45)
_cons	-0.00853	-0.0520**	-0.0628***	-0.0583	-0.0170
	(-0.50)	(-3.09)	(-3.85)	(-1.71)	(-0.40)
r2_a	-0.00569	-0.00888	0.00496	-0.0155	-0.0154
N	108	194	194	105	120

Notes: *T* statistics in parentheses - * $p < 0.05$, ** $p < 0.01$, *** $p < 0.001$. Returns are winsorized at the 1% level.

IV. THE ODDNESS OF THE SPAC LITIGATION DELUGE

The punchline result from my sample is an intuitively paradoxical one: that the likelihood of being sued *increases* for SPACs with lower redemption rates. One might more naturally expect to see lawsuits arising from de-SPAC transactions of lower quality; a high redemption rate would signal that the SPAC investors lack confidence in the proposed merger, and thus that the deal is likely to be worse. Intuitively, it seems that this should generate more lawsuits, not fewer.

There are several possible explanations for this result. First, it is possible that the transactions drawing lawsuits do, in fact, involve fraud. The fraud could induce investors not to redeem, meaning that the low redemption rates reflect the fact that shareholders were lied to, rather than the quality of the deal. This thesis is complicated somewhat by the fact that roughly half of the claims in my sample are merger objection claims that were brought

62. I emphasize here that the sample of 10b-5 claims is small, so these results may lack predictive power.

before the transaction closed and shareholders redeemed their shares. In this scenario, it is possible that the lawsuit revealed the fraud and actually induced truthful disclosures that strengthened investors' confidence in the deal, thereby inducing them not to redeem. Finally, it is possible that that plaintiffs are not targeting SPACs involving fraud, and the negative association between litigation likelihood and redemption rate arises for reasons unrelated to the quality of de-SPAC deals as measured by redemption rate. I assess each of these possibilities below.

A. SPAC Litigation Targets Fraudulent Transactions

One possible explanation for the negative association between the likelihood of a lawsuit and redemption rate is that the transactions that are challenged involve misrepresentations. If the management lies to its shareholders about the quality of its target and diligence, the shareholders may be confident that the deal is a good one and decline to redeem their shares—but this confidence is misplaced. The discovery of such misrepresentations could give rise to lawsuits even where shareholder redemption rates are low.

1. Post-Closing Lawsuits: (Mostly) Rule 10b-5

This seems like a straightforward explanation for SPAC-related lawsuits that are brought after the transaction closes. The majority of such claims in my sample are brought under Rule 10b-5.[63] These claims generally allege a sequence of misconduct that began before the merger and continued through the de-SPAC transaction. Although the recency of the litigation makes it difficult to assess, there are some early signs that these cases may have merit. While half of the merger objection lawsuits in my sample were voluntarily dismissed within the sample period, only a single lawsuit containing a 10b-5 claim was dismissed (out of fifty-three 10b-5 claims). The 10b-5 lawsuits appear to target the de-SPAC transactions with the youngest target companies and the shortest completion timelines, potentially indicating risky business combinations or subpar diligence. Moreover, this is the area in which highly ranked plaintiffs' law firms have become involved in SPAC-related litigation. The top ranked firms in my sample filed nineteen Rule 10b-5 claims, as compared with four 14(a) claims and four fiduciary duty claims. However, because so few outcomes are available as a result of the longer litigation timeline for these cases, it is difficult to evaluate their

63. Only twenty-two merger objection claims in my sample are brought after the merger. Of these twenty-two claims, eleven are bundled with 10b-5 claims, leaving only eleven standalone post-closing merger objection claims. By contrast, all forty-nine out of fifty-three Rule 10b-5 claims in my sample are brought after the merger.

quality. The Rule 10b-5 claims in my sample also usually involve defendant SPACs with the highest IPO proceeds (often associated with higher quality deals).[64] The average redemption rate of deals that draw 10b-5 lawsuits is only 14.5%. And finally, I find no statistically significant association between 10b-5 claims and returns on deals in any period. While this finding could be affected by the size of the sample and the availability of information, it may suggest that such lawsuits do not focus on the deals in which investors made out the worst.

There also appear (perhaps unsurprisingly) to be links between Rule 10b-5 claims and public enforcement regarding SPACs.[65] Rule 10b-5 claims began to climb in earnest in the first half of 2021, when the SEC announced that it would be scrutinizing SPAC deals more carefully.[66] This may simply indicate that plaintiffs' lawyers are jumping on enforcement guidance to make their claims more plausible. However, of the three de-SPAC transactions that have so far generated SEC enforcement actions, two had previously generated multiple Rule 10b-5 lawsuits. The merger between SPAC Diamond Peak Holdings and Lordstown Motors drew SEC and Department of Justice probes in July 2021.[67] The deal, which was completed in October of the previous year, had already generated six Rule 10b-5 lawsuits by the end of the sample period. Similarly, the merger between SPAC VectoIQ and Nikola, which culminated in fraud charges against the combined company's CEO in July 2021,[68] had drawn three Rule 10b-5 lawsuits during the sample period since its closing in June 2020.[69] Because

64. *See* Bazerman & Patel, *supra* note 1, at 110.

65. *See* Emily Strauss, *Is Everything Securities Fraud?*, 12 U.C. IRVINE L. REV. 1331, 1338 (2022).

66. *See, e.g.*, Mark Schoeff Jr., *Booming SPAC Market Draws SEC Scrutiny*, INVESTMENTNEWS (Mar. 11, 2021), https://www.investmentnews.com/booming-spac-market-draws-sec-scrutiny-203844 [https://perma.cc/MF4N-WL6Y]; Jody Godoy & Chris Prentice, *U.S. Regulator Opens Inquiry into Wall Street's Blank Check IPO Frenzy—Sources*, REUTERS (Mar. 24, 2021), https://www.reuters.com/article/us-usa-sec-spacs-exclusive/exclusive-u-s-regulator-opens-inquiry-into-wall-streets-blank-check-ipo-frenzy-sources-idUSKBN2BH09F [https://perma.cc/Q4XE-A3XR]; Chris Katje, *New SEC Chair Gary Gensler Could Push For SPAC Regulation*, YAHOO! FIN. (Jan. 20, 2021), https://finance.yahoo.com/news/sec-chair-gary-gensler-could-202602323.html [https://perma.cc/93TK-M4US]; Press Release, John Coates, Acting Dir., Div. Corp. Fin., U.S. Sec. & Exch. Comm'n, SPACs, IPOs & Liability Risks under the Securities Laws, (Apr. 8, 2021), https://www.sec.gov/news/public-statement/spacs-ipos-liability-risk-under-securities-laws [https://perma.cc/W2FC-AD76].

67. Ben Foldy, *Lordstown Motors Discloses Justice Department Investigation as Truck Launch Looms*, WALL ST. J. (July 16, 2021), https://www.wsj.com/articles/electric-truck-startup-lordstown-motors-discloses-justice-department-investigation-11626443066 [https://perma.cc/7SZN-4FM6].

68. Press Release, U.S. Sec. & Exch. Comm'n, SEC Charges Founder of Nikola Corp. with Fraud (July 20, 2021), https://www.sec.gov/news/press-release/2021-141 [https://perma.cc/L4Q8-599Y].

69. The third SPAC deal scrutinized by the SEC, between Stable Road Acquisition Company and Momentus, did not close during the sample period or prior to the SEC's charges of misleading disclosures ahead of the merger, and accordingly generated only a single Rule 14a-9 lawsuit in my sample. *See* Press

the SEC is resource constrained, it is commonly thought that the charges it pursues have a high likelihood of merit.[70] That Rule 10b-5 lawsuits arose in significant quantity for these deals before the SEC inquiries suggests that plaintiffs' lawyers in those specific cases were onto something and that at least in some instances, these lawsuits actually penalize misconduct.[71]

Though they comprise a minority of claims brought after the transaction, I note that there are also some early signs that at least some of the post-closing merger objections in my sample may have teeth. These claims consist of Rule 14a-9 claims alleging proxy fraud and state fiduciary duty claims (often, they are bundled together). Traditionally, post-closing lawsuits for breach of state fiduciary duty are brought by target shareholders alleging that they received an insufficient price for their shares. Analogous claims brought by SPAC shareholders, however, are acquirer shareholder claims, alleging that SPAC directors breached their fiduciary duties by allowing the SPAC to *overpay* for the target. In the absence of conflicts, such lawsuits are subject to the business judgment rule. This may explain why relatively few of the post-closing fiduciary duty lawsuits in my sample are couched in these terms. Rather, most of the post-closing fiduciary duty claims in my sample allege that the SPAC directors breached their duty of oversight by permitting the fraudulent statements alleged in the proxy.

One notable exception is *In re Multiplan Stockholder Litigation*[72] in the Delaware Chancery Court. The case arose out of a transaction between Churchill, the SPAC, and Multiplan, a healthcare data analytics provider.[73] The crux of the SPAC shareholders' allegations was that Multiplan's largest customer, on which it was dependent, was forming an in-house competitor and planned to shift its business away from Multiplan, and that Churchill's board deliberately failed to disclose this information in the proxy.[74] The complaint alleged that the SPAC directors, who were all appointed by and had previous ties with the SPAC sponsor, violated their fiduciary duties by

Release, U.S. Sec. & Exch. Comm'n, SEC Charges SPAC, Sponsor, Merger Target, & CEOs for Misleading Disclosures Ahead of Proposed Business Combination (July 13, 2021), https://www.sec.gov/news/press-release/2021-124 [https://perma.cc/L4Q8-599Y].

70. James D. Cox, Randall S. Thomas & Dana Kiku, *SEC Enforcement Heuristics: An Empirical Inquiry*, 53 DUKE L.J. 737, 763 (2003).

71. In both cases, the misstatements were initially brought to light by short-seller reports. *See The Lordstown Motors Mirage: Fake Orders, Undisclosed Production Hurdles, and a Prototype Inferno*, HINDENBERG RSCH. (Mar. 12, 2021), https://hindenburgresearch.com/lordstown [https://perma.cc/24XK-Y6UW]; Ben Foldy, *Nikola Internal Review Confirms Some Claims in Short Seller's Report*, WALL ST. J. (Feb. 26, 2021), https://www.wsj.com/articles/nikola-internal-review-confirms-some-claims-in-short-sellers-report-11614350745 [https://perma.cc/N9YP-8SDV].

72. *See generally In re* MultiPlan Corp. S'holders Litig., 268 A.3d 784 (Del. Ch. 2022).

73. *Id.* at 792.

74. *Id.* at 797.

"issuing a false and misleading proxy, harming stockholders who could not exercise their redemption rights on an informed basis."[75] In a widely cited opinion, Vice Chancellor Lori Will denied the directors' motion to dismiss the claims against the SPAC board and sponsor, finding that the claims were direct, rather than derivative, and therefore plaintiffs need not plead demand futility, and that the board conflicts meant that the transaction would be reviewed under the demanding entire fairness standard.[76] If these determinations hold after trial, they will likely be powerful tools for SPAC investors alleging that they were lied to in connection with a de-SPAC merger. The entire fairness standard only applies where there is a conflict of interest, but SPAC sponsors may often be conflicted, and where sponsors appoint boards with which they have financial ties, as they often do,[77] the threat of entire fairness review is likely to have bite. Moreover, unlike Rule 10b-5 lawsuits, which often take years to resolve, fiduciary duty cases in the Delaware Chancery Court are likely to move relatively quickly, suggesting that these may be the cases most likely to curb SPAC misconduct in the immediate future.

2. Pre-Closing Lawsuits: Merger Objection Claims

Pre-closing merger objection claims are a different beast from most Rule 10b-5 litigation. Much merger objection litigation is disposed of before the closing of the transaction. Thus, the effects of pre-closing merger objection litigation on de-SPAC transactions may, in theory, be quite direct; specific deals may be halted, or management may release additional information pertaining to specific aspects of the deal, giving shareholders greater confidence (or not, as the case may be). Rule 10b-5 litigation, by contrast, is notoriously slow, often taking years to be resolved.[78]

The characteristics of transactions that drew the Rule 14a-9 and state fiduciary duty claims in my sample are reported in Table 4. I note that state fiduciary duty claim defendants boast the lowest mean redemption rate of the claim types in my sample at 13.44% (Rule 14a-9 claims correspond with slightly higher redemption rates, at 18.73%). De-SPAC transactions that are

75. *Id.* at 800. The fewer shareholders redeem their shares, the more valuable the sponsor shares will be after the merger, because (1) the resulting entity will be more liquid; and (2) the sponsor shares will be less diluted. *See* Klausner & Ohlrogge, *supra* note 39, at 6.

76. *MultiPlan*, 268 A.3d at 805, 818.

77. *See* Klausner & Ohlrogge, *supra* note 39, at 5–6.

78. *See* LAARNI T. BULAN & LAURA E. SIMMONS, CORNERSTONE RSCH., SECURITIES CLASS ACTION SETTLEMENTS: 2021 REVIEW AND ANALYSIS 13 (2021), https://www.cornerstone.com/wp-content/uploads/2022/03/Securities-Class-Action-Settlements-2021-Review-and-Analysis.pdf [https://perma.cc/4VPS-DAY8] (finding that more than 40% of securities class actions take between three and four years to settle).

targeted by state fiduciary duty lawsuits have a higher mean enterprise value but lower IPO proceeds than those of Rule 14a-9 claims. They also issue fewer warrants, and the target companies are slightly older. All this indicates that along most metrics (redemption rate, warrants, and target age), lawsuits alleging breaches of state fiduciary duties tend to target de-SPAC transactions that generally appear to be higher quality deals.

If fraud explains the association between rising litigation likelihood and falling redemption rates, the merit of the pre-closing claims in my sample is complicated to assess. The redemption rate in de-SPAC transactions is tabulated very near the closing of the transaction, so redemption rates should, in theory, incorporate any information revealed in a pre-closing lawsuit. Accordingly, these lawsuits could be having one of two effects. First, it is possible that the pre-closing merger objection claims in my sample are halting some bad transactions and lowering redemption rates in deals that close by giving investors greater confidence in the deal. This could be the result of the supplemental disclosures that many defendants issue in response to merger objection litigation. These supplemental disclosures could correct any misrepresentations or omissions and make investors feel good about retaining their shares. In the best case, these disclosures could prompt heightened diligence in management's pursuit of the deal. The second possibility is less rosy; merger objection claims could target fraudulent transactions, but nonetheless fail to induce investors to redeem, either because investors do not perceive these lawsuits to credibly signal fraud, or because SPAC managers, undeterred by the monetary and reputational consequences of these lawsuits, continue to lie to their investors. While merger objection claims are theoretically a promising means of improving de-SPAC transactions before they close, I argue that they do not appear to be fulfilling this role. If fraud causes investors to sue but prevents shareholders from redeeming, I argue that the more plausible explanation for the negative association between the likelihood of pre-closing merger litigation and redemption rate is that these lawsuits fail to induce investors to redeem their shares, or SPACs to be more truthful in their disclosures.[79]

Merger objection litigation over the last decade has been aptly described as "schizophrenic."[80] At its peak in 2013, a whopping 96% of announced mergers gave rise to litigation by investors, and 60% of the

79. I note that all sued de-SPAC transactions in my sample closed, meaning that pre-closing merger challenges did not halt any deals, bad or otherwise.

80. *See* Cain et al., *Mootness Fees*, *supra* note 11, at 1779. For discussion of shareholder litigation challenging director conduct in mergers in prior years, see Robert B. Thompson and Randall S. Thomas, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133, 134–41 (2004).

lawsuits were filed in the Delaware Chancery Court.[81] These lawsuits drew widespread criticism on the ground that they largely lacked merit and that settlements were generally for pre-merger supplemental disclosures that did not benefit shareholders, but did generate lucrative fees for plaintiffs' lawyers.[82] In January 2016, the Delaware Chancery Court cracked down on these lawsuits in what proved to be a landmark decision, *In re Trulia*.[83] In that decision, the court declared its refusal to approve settlements in merger cases that do not provide "[m]eaningful [b]enefit" to shareholders.[84]

The literature has demonstrated that the effect of *Trulia*, in addition to other concurrent cases raising the bar that plaintiffs must meet in merger objection cases,[85] was a plummet in the number of merger objection cases filed in Delaware.[86] To prevent plaintiffs from merely fleeing to other state courts, Delaware's legislature also allowed for the adoption of forum selection bylaws prohibiting lawsuits in other states.[87] However, these provisions do not extend to Exchange Act claims in federal courts, and accompanying the drop in Delaware cases was a marked increase in merger-related lawsuits filed in the federal courts under Rule 14a-9. By 2018, one account found that only 9% of merger-related lawsuits were brought in Delaware, while 87% were brought in federal court.[88]

In addition to circumventing Delaware's strictures on merger litigation jurisdictionally, plaintiffs' lawyers have also found creative ways to avoid the constraints on settlements for window-dressing disclosures and lawyers' fees. Following *Trulia* dicta, many defendants have begun to make voluntary supplemental disclosures in response to merger objection lawsuits, thus rendering the claims moot, and paying plaintiffs' counsel a mootness fee as long as those disclosures were of benefit to shareholders (even if not material to the vote).[89] Various commentators, including courts, have expressed

81. Cain et al., *Mootness Fees*, *supra* note 11, at 1779.

82. *See* Cain et al., *Shifting Tides*, *supra* note 11, at 605; Gregory A. Markel & Gillian G. Burns, *Assessing a Judicial Solution to Abusive Merger Litigation*, LAW360 (Nov. 19, 2015, 9:59 AM), https://www.law360.com/articles/728061/assessing-a-judicial-solution-to-abusive-merger-litigation [https://perma.cc/BT7Q-KG3T].

83. *In re* Trulia, 129 A.3d 884, 899 (Del. Ch. 2016).

84. *Id.*

85. *See e.g.*, Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304, 305–06 (Del. 2015); *In re* Volcano Corp., 143 A.3d 727, 750 (Del. Ch. 2016).

86. *See* Cain et al., *Shifting Tides*, *supra* note 11, at 608; *see also* James D. Cox & Randall S. Thomas, *Delaware's Retreat: Exploring Developing Fissures and Tectonic Shifts in Delaware Corporate Law*, 42 DEL. J. CORP. L. 323, 326 (2018).

87. Cox & Thomas, *supra* note 86, at 325.

88. *See* Cain et al., *Shifting Tides*, *supra* note 11, at 608.

89. Cain et al., *Mootness Fees*, *supra*, note 11, at 1780 (alteration in original). The authors note that mootness fees are not always disclosed by the parties, and therefore their data may be underinclusive.

skepticism about this practice, claiming that the supplemental disclosures in contemporary merger litigation confer no real benefit on shareholders.[90] Nonetheless, a recent study has found that at least 63% of merger cases were disposed of with a mootness fee and that such fees appear to have entirely replaced formal settlements in merger objection cases in federal court.[91]

To investigate whether pre-closing merger objection claims improve de-SPAC transactions, I run unreported regressions in which the dependent variables are the three-day, seven-day, fourteen-day, thirty-day, and ninety-day returns on the deal,[92] and the independent variable is a dummy equal to one if the transaction generated at least one pre-closing merger objection claim, controlling for target age. There is no statistically significant association in any specification. Thus, there is no evidence that transactions that draw a pre-closing merger objection claim perform better in the first three months than transactions that draw no lawsuits.

To assess the role of the supplemental disclosures that may be prompted by merger challenges, I use SEC EDGAR and internet searches to see whether defendant SPACs voluntarily released additional disclosures in response to pre-closing lawsuits. In my sample, defendant SPACs issued supplemental disclosures in response to pre-closing merger objection lawsuits 46.15% of the time. The average redemption rate of the de-SPAC transactions that were sued prior to the merger that did not issue supplemental disclosures is 19.11%, while the average redemption rate for those that did issue supplemental disclosures is 6.78%. However, this difference is not statistically significant.[93] The rate of supplemental disclosures in my sample appears to be substantially lower than that which other studies have documented regarding deal litigation in federal courts.[94] Half of the merger objection cases in my sample were voluntarily dismissed by the end of the sample period. Roughly half of those dismissals involved defendant SPACs that appear to have made no supplemental disclosures at all.

Id. at 1791 n.41; *see also In re* Xoom Corp., S'holder Litig., No. 11263-VCG, 2016 Del. Ch. LEXIS 117, at *14–15 (Del. Ch. Aug. 4, 2016) (awarding a $50,000 mootness fee and holding that *Trulia*'s materiality requirement did not apply to mootness fees).

90. *See, e.g.*, *In re* Walgreen Co., 832 F.3d 718, 721, 725–26 (7th Cir. 2016).

91. Cain et al., *Mootness Fees*, *supra* note 11, at 1782.

92. Returns are winsorized at the 1% level.

93. The t-statistic is 1.4127. I note that the mean redemption rate for transactions in which no supplementary disclosures were issued may be driven by two particularly high-redemption deals, the Blackridge Acquisition Corporation/Ourgame International merger (88.9%) and the Boxwood Merger Corporation/Atlas TC Holdings merger (94.9%). Without these outliers, the mean redemption rate of SPACs that did not issue supplemental disclosures is 14.26%, and the t-statistic is 1.047.

94. Cain et al., *Mootness Fees*, *supra* note 11, at 1782 (finding mootness fees paid in 63% of litigated deal cases in federal court in 2018; the mootness fees are purported compensation for obtaining supplemental disclosures).

I also use SEC EDGAR and internet searches to examine the fees paid by SPACs in connection to these lawsuits. These fees are generally immaterial to the defendant companies that pay them and therefore are often not widely disclosed.[95] They also involve dismissal before certification of a putative class and are therefore not subject to approval by courts[96] (unsurprisingly, none of the merger objections in my sample involve on-the-docket settlements). Very few of the transactions in my sample disclosed mootness fees paid in connection with lawsuits; the average amount was $200,000. This is in line with estimates from other studies, which have found that mootness fees range in amount from $200,000 to $450,000 but have declined in more recent years.[97]

There are two likely overlapping possibilities for why these lawsuits might not induce SPAC shareholders to redeem their shares, even if they target transactions that involve misrepresentations. First, shareholders may not believe that these lawsuits credibly signal fraud. Their ubiquity may mean that investors simply do not take these lawsuits seriously. The disclosures they prompt may not seem to add anything important. Previous literature has concluded that, even when they are made, the supplemental disclosures of yore did not influence shareholder voting outcomes,[98] and the current disclosures required in exchange for mootness fees need not even be material.[99] The amounts that SPAC defendants pay to make these lawsuits go away may not seem to investors like a penalty to remedy serious wrongdoing, but an added tax to make sure the deal closes on time.

There are other reasons that these pre-closing merger objections may not signal to investors that something is truly amiss. More than half (57%) of the merger objection lawsuits brought in New York Supreme Court are against SPACs that have a forum selection clause in the charter or bylaws delegating Delaware as the forum for any fiduciary duty litigation.[100] Of these, 76% were voluntarily dismissed within the sample period without litigation, suggesting two possibilities: (1) the plaintiffs filed first and researched the defendant firms later, discovering the forum selection

95. Gregory A. Markel, Vincent A. Sama, Catherine B. Schumacher & Daphne Morduchowitz, *Over 50 M&A Deals Have Been Challenged this Year by a Single Group of Lawyers*, LEXOLOGY (June 12, 2020), https://www.lexology.com/library/detail.aspx?g=f275b650-6822-4bc1-9e56-0314b51dd760 [https://perma.cc/EN7Y-FEX3].

96. *Id.*

97. Cain et al., *Mootness Fees*, *supra* note 11, at 1803.

98. *See* Cain et al., *Shifting Tides*, *supra* note 11, at 605.

99. Cain et al., *Mootness Fees*, *supra* note 11, at 1780.

100. I also note that some of the SPACs drawing pre-closing merger objections are, like many SPACs, incorporated in the Caymans, meaning that they would not be subject to the fiduciary duties of any state.

provisions after the lawsuits were filed and then voluntarily dismissed them; or (2) the plaintiffs privately demanded fees from the defendant SPACs in return for withdrawal that were lower than the cost of litigating the forum selection provision, suggesting that the fees, and thus the settlement value of these cases, were very low. Neither option inspires confidence in the quality of these lawsuits.

Furthermore, the most frequently filing law firms' litigation patterns in my sample suggest that these cases may not represent credible signals of misconduct. I report the plaintiff firms in my sample in Table 5. The three most frequently-filing plaintiffs' firms in my sample—Brodsky Smith, Monteverde & Associates, and Rigrodsky Law—account for just over 40% of the lawsuits in my sample. These frequent filers appear to be small plaintiffs' firms of between five and eight lawyers. Their prolific but largely unlitigated filings have been noted in other studies,[101] leading commentators to remark that "these law firms appear to be more interested in collecting mootness fees than in actively litigating the cases that they file."[102] Moreover, the complaints filed in the New York Supreme Court, as noted by other commentators,[103] purport to seek an injunction blocking the merger, but do not include the separate motions for a preliminary injunction that would actually be necessary to put off the shareholder vote.[104] This account of entrepreneurial SPAC firms is consistent with many assessments in the literature of plaintiffs' lawyers' behavior in the securities and corporate context. One study postulates that the passage of the Private Securities Litigation Reform Act of 1994 ("PSLRA"), and the higher expenses involved in meeting its pleading standards, pushed many small firms away from 10b-5 class actions and toward corporate litigation, such as that challenging mergers.[105] Others note the rise in dismissals (used as a proxy

101. Cain et al., *Mootness Fees*, *supra* note 11, at 1798–99 (finding each of these firms in the top six filers of federal merger lawsuits in 2017–2018). I note that most cases in my sample filed by Rigrodsky Law and Brodsky Smith are in fact fiduciary duty claims filed in the New York Supreme Court, implying that the total number of lawsuits filed by these firms is larger than reported in either study. *See also* Alison Frankel, *Rigrodsky Puts Controversial 'Mootness Fee' Business Model under Scrutiny*, REUTERS (Oct. 13, 2021), https://www.reuters.com/legal/transactional/rigrodsky-puts-controversial-mootness-fee-business-model-under-scrutiny-2021-10-13 [https://perma.cc/X6MC-9CKQ].

102. Cain et al., *Mootness Fees*, *supra* note 11, at 1799 (noting that the top six frequent filers settled only 1%–4% of their cases, but appeared to collect mootness fees in 65%–80%).

103. Frankel, *supra* note 7; Kevin LaCroix, *SPAC-Related State Court Merger Objection Litigation*, D&O DIARY (May 9, 2021), https://www.dandodiary.com/2021/05/articles/merger-litigation/spac-related-state-court-merger-objection-litigation [https://perma.cc/BEU4-8EMD].

104. These commentators note that the filings on the docket are only "part of the story" and that defendant firms frequently receive demand letters for fees before filing a complaint. Frankel, *supra* note 101.

105. Brian Cheffins, John Armour & Bernard Black, *Delaware Corporate Litigation and the Fragmentation of the Plaintiffs' Bar*, 2012 COLUM. BUS. L. REV. 427, 431 (2012).

for low-quality cases) concurrent with the rise in lawsuits brought by "emerging firms" in the securities arena generally.[106] Still others have noted that plaintiffs' firms have proven resilient to attempts to crack down on nuisance litigation and have circumvented these efforts, particularly in the merger litigation context, by filing in federal courts or jurisdictions outside Delaware and by evading requirements for more useful disclosures by voluntarily dismissing cases in exchange for mootness fees.[107]

The second reason that these lawsuits may not induce shareholders to redeem even if they target truly fraudulent transactions is that the fees paid to plaintiffs' attorneys may be unlikely to deter such fraud. Unscrupulous SPAC managers could pay $200,000, issue supplemental disclosures, and *continue to lie* about the quality of the target or the diligence they conducted in order to close the transaction and receive their 20% promote. This may contrast with more traditional IPO litigation under section 11, as discussed in Section III.B.

Many of the regulatory and scholarly concerns for the welfare of SPAC investors revolve around issues that might be mitigated with improved disclosure, such as conflicts of interest, speedy deal process, and dilution. Pre-merger deal litigation could theoretically be a mechanism well-suited for providing greater transparency to investors. However, there are reasons to think that even if these cases are targeting fraudulent transactions, they fail to induce SPAC shareholders to redeem. If true, this explanation is a strong condemnation of merger litigation generally, and even more so in the SPAC context: in transactions that are known to be risky to investors, that are by their nature fraught with conflicts of interest, and in which fraud could plausibly be rampant, the type of lawsuit that, in theory, could be of the most preemptive benefit to shareholders is being leveraged by a small number of small firms for small fees at investors' expense.

B. SPAC-RELATED LITIGATION IS UNRELATED TO TRANSACTION QUALITY

Of course, it is possible that the SPAC-related lawsuits in my sample do not target fraudulent transactions, and that the lower redemption rates of the transactions that appear to draw lawsuits are not the product of misrepresentations. If this is the case, it appears that plaintiffs may simply have chosen lower-redemption SPACs to sue. The probability of being sued appears to be related neither to the size of the deal, nor the returns, nor the

106. Klausner & Heglund, *supra* note 55.

107. *See* Cain et al., *Shifting Tides*, *supra* note 11, at 607; Cain et al., *Mootness Fees*, *supra* note 11, at 1781.

industry, nor the management. Accordingly, in the absence of fraud, we can say little more than that these lawsuits do not appear to be logically related to common metrics for transaction quality, including redemption rate.

There is some reason to think that not all of the low-redemption deals which appear more likely to draw lawsuits involve fraud. My sample suggests that the boom year for redemptions was 2019, with a mean redemption rate of 64.96% across all de-SPAC transactions completed that year. However, only nine SPAC-related lawsuits were filed. The mean redemption rate declined to 37.45% in 2020 as lawsuits climbed to forty-six and even further in the first half of 2021 to 22.98%, as lawsuits exploded at a whopping eighty-nine. Significantly, the first half of 2021 was also the time when the SEC, under the then-new Biden administration, began publicly to take aim at SPACs. The end of March and early April 2021 saw a highly publicized cluster of SEC releases and statements specifically geared at SPACs, addressing, among other issues, key filing issues,[108] accounting considerations,[109] and liability risk under the securities laws.[110] By the end of April, reports were circulating that the SEC was considering new guidance on SPACs.[111] If fraud is the explanation for low redemption rates, then conversely, SPACs reporting high redemption rates are the ones that told the unpromising truth about their prospects and diligence, causing investors to redeem. But according to my sample, these candid, high-redemption SPACs proliferated in earlier years, while SPACs reporting the lowest redemption rates (resulting, presumably, from lying to their shareholders) [112] did their

108. *See, e.g.*, Press Release, U.S. Sec & Exch. Comm'n Div. Corp. Fin., *supra* note 36.

109. *See, e.g.*, Press Release, John Coates, Acting Chief Div. Corp. Fin., & Paul Munter, Acting Chief Acct., U.S. Sec & Exch. Comm'n, Considerations for Warrants Issued by Special Purpose Acquisition Companies ("SPACs") (Apr. 21, 2021), https://www.sec.gov/news/public-statement/accounting-reporting-warrants-issued-spacs#_ftnref3 [https://perma.cc/A8N4-Y3B6].

110. *See, e.g.*, Press Release by John Coates, *supra* note 66.

111. Anirban Sen, Chris Prentice & Joshua Franklin, *Exclusive U.S. Watchdog Mulls Guidance to Curb SPAC Projections, Liability Shield –Sources*, REUTERS (Apr. 27, 2021), https://www.reuters.com/business/exclusive-us-watchdog-weighs-guidance-aimed-curbing-spac-projections-liability-2021-04-27 [https://perma.cc/XDF4-WHYT].

112. Some commentators have provided other explanations for the improvement in SPAC redemption rates over time. Some commentators postulate that the SPAC market is "self-correcting" because of demands from institutional investors; some structural changes include the size and nature of the sponsors' "promote" and the length of time sponsors are required to hold their shares following the de-SPAC transaction. *Going Public: SPACs, Direct Listings, Public Offerings, and the Need for Investor Protections: Hearing Before the Subcomm. on Inv. Prot., Entrepreneurship & Cap. Mkts. of the H. Comm. on Fin. Servs.*, 117th Cong. 10–11 (2021) (statement of Scott Kupor, Managing Partner, Andreessen Horowitz), https://financialservices.house.gov/uploadedfiles/hhrg-117-ba16-wstate-kupors-20210524.pdf?te=1&nl=dealbook&emc=edit_dk_20210524 [https://perma.cc/E9VL-GXUE]. Others state that "SPAC sponsors today are more reputable than they have ever been, and as a result, the quality of their targets has improved, as has their investment performance." Bazerman & Patel, *supra* note 1, at 105. Sponsors have also been increasing their contributions to the merger and decreased the number of

lying concurrently—at least in part—with the announcement that regulatory scrutiny of SPACs was significantly on the rise. It seems counterintuitive that SPACs would be honest when no one was looking and engage in fraud just as the SEC announced that it would be looking very carefully.

To be sure, there is not complete alignment of timing—the SEC's statements did not begin until April, meaning that SPACs closing earlier in 2021 would have no reason to be more truthful with their investors (other than the ascension of a more pro-regulation administration) than the SPACs before them. However, there may be some explanations for the relationship between redemption rate and lawsuit probability that do not involve fraud.

1. Post-Closing Lawsuits: Standing and Class Size

One potential explanation for the negative relationship between the probability of a lawsuit and redemption rate may be putative class size. In a post-closing lawsuit, fewer redeeming shareholders could mean a larger potential class of investors, which would presumably result in more damages, greater pressure to settle, and a larger potential payout, and therefore a more lucrative lawsuit for plaintiffs' counsel.

This line of reasoning operates slightly differently for the different types of claims in my sample. Most directly, shareholders have standing in Delaware to challenge a merger under laws of fiduciary duty only if they owned stock at the time of the challenged transaction and throughout the litigation.[113] This means that shareholders who redeem their shares before the merger are clearly out. Similarly, private plaintiffs are presumed to have standing under Rule 14a-9 if they were injured in connection with a proxy solicitation and if "reliance of some shareholders on the statement was likely to affect [how they voted]."[114] Shareholders in SPACs can vote for the transaction and still redeem their shares, but in such a situation are unlikely to have been injured.[115]

warrants they offer per unit at the IPO, which makes the de-SPAC transaction less dilutive. *See* Gahng et al., *supra* note 12, at 33.

113. Christopher M. Harvey, *Corporate Law—Mergers and Double Derivative Actions: The New Frontiers in Derivative Standing*, 38 VILL. L. REV. 1194, 1196–97 (1993).

114. THOMAS LEE HAZEN, FEDERAL SECURITIES LAW 94 (2d ed. 2003).

115. It appears to be unsettled whether the presumption of reliance on the proxy is rebuttable. *See, e.g.*, Dowling v. Narragansett Cap. Corp., 735 F. Supp. 1105, 1120 (D.R.I. 1990) ("[T]hat presumption [of reliance on the proxy] may be rebutted by evidence that the alleged misinformation had no effect on the action taken."); Gaines v. Haughton, 645 F.2d 761, 774 (9th Cir. 1981) ("[S]hareholders who do not rely on allegedly misleading or deceptive proxy solicitations lack standing to assert direct (as opposed to derivative) equitable actions under § 14(a)."); Philip B. Kurland, *The Supreme Court, 1963 Term*, 78 HARV. L. REV., 143, 299 (1964) ("A rebuttable presumption of shareholder reliance is necessary, for it would be impossible to show the effect of such violations on those who gave the proxies."). *But see*

Plaintiffs have standing under Rule 10b-5 if they purchased or sold securities in connection with manipulative or deceptive conduct.[116] Such a class could encompass investors who bought the shares of the merged company on the secondary market in reliance on misleading statements issued before or in connection with the merger. Nonetheless, a large class of non-redeeming shareholders who bought their shares based on rosy statements about the deal could also form the basis of a lucrative class for an action under Rule 10b-5.[117]

If class size is the explanation for the negative relationship between litigation probability and redemption rate, then these cases may be opportunistic, rather than targeting the worst transactions. Larger classes likely involve larger damages, create the shadow of greater potential liability, and thus are likely to induce greater pressure to settle and probably a larger payout for plaintiffs' lawyers.[118] This may also be an explanation for the greater involvement of top tier plaintiffs' lawyers that does not rely on merit; these firms generally have relationships with institutional investors who are well-positioned to be lead plaintiff in Rule 10b-5 class actions if they want to be and may deliberately target these cases based on potential payoff.

2. Pre-Closing Lawsuits: Litigation as a Substitute or Complement for Redemption

One possible explanation of the negative relationship between litigation and redemption rate in de-SPAC transactions for pre-closing merger challenges that does not involve fraud may be that SPAC shareholders are increasingly using litigation as a substitute or complement for exercising their redemption rights.

On its face, using litigation as a substitute for redemption makes little sense. The SPAC shareholders' redemption right is essentially a free put option, allowing shareholders to costlessly back out of the transaction.

Sandberg v. Va. Bankshares, Inc., 891 F.2d 1112, 1120 (4th Cir. 1989) ("[T]he rebuttable presumption in § 10(b) actions is not applicable to § 14(a) actions."). However, it is an interesting question whether such a presumption could be rebutted with respect to SPAC shareholders who redeem their shares but vote for the transaction.

116. Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 749 (1975).

117. The average time elapsed between the merger and the end of the class period for Rule 10b-5 claims in my sample is roughly 6 months, although this falls to 4.7 months if I remove 2 extremely long outliers.

118. Lisa L. Casey, *Reforming Securities Class Actions from the Bench: Judging Fiduciaries and Fiduciary Judging*, 2003 BYU L. REV. 1239, 1239, 1241 (2003) ("Certainly the lawsuits hold the promise of enormous potential profits for class counsel. As a general matter, the larger the company sued (as measured by market capitalization), the larger the losses suffered by the putative class, and the larger the potential settlement fund.").

Moreover, many redeeming shareholders do not entirely surrender their claims to the company should the merger prove to be a good one—they may keep their warrants and vote for the transaction, even if they choose to redeem their shares.

To be sure, freeriding on a lawsuit is also a costless option. There appears to be little downside to a nonplaintiff shareholder to watching such a lawsuit unfold. In the context of pre-closing merger objection litigation, any supplemental disclosures may improve deal quality (although, as discussed, this is unlikely), and although the sample is small, my results indicate that share prices of the merged company do not appear to suffer as a result of pre-closing merger challenges. But while the occasional shareholder may actually believe that a merger objection claim will increase the value of their post-merger shares, this appears unlikely based on the supplemental disclosures issued in my sample and given the dysfunctionality of much merger litigation generally. Indeed, it appears that many of these lawsuits are driven by plaintiffs' lawyers in exchange for nominal fees rather than by SPAC shareholders. Accordingly, it seems generally improbable that the negative relationship between the likelihood of a lawsuit and redemption rate is the result of shareholders treating these options as substitutes.

It might also be possible that sophisticated investors, who may be more likely to redeem,[119] are also more likely to sue as a means of extracting the most possible value from their shares. Although the most direct monetary gains would result if redeeming investors could bring post-closing lawsuits for damages, they generally lack standing to do this. It is also possible that sophisticated investors who redeem might bring pre-closing lawsuits in the hopes of improving the transaction and thus upping the value of their warrants (which they can retain through redemption). I note, however, that the vast majority of merger objection claims in my sample are brought by individual investors, rather than the institutional ones more likely to engage in sophisticated strategy. It is therefore not clear that litigation is being used as a complement to the redemption right intended to make money.

119. This raises a related possibility for the inverse association between redemption rate and litigation probability: investor composition. Anecdotally, the composition of SPAC investors changed significantly over the course of the boom. Prior to 2019, SPACs were a niche market. Investors in them were sufficiently sophisticated both to understand what they were getting and also to exercise their redemption rights when what they got fell short of what they were promised. However, accounts from lawyers suggest that as SPACs went mainstream in 2020 and throughout 2021, the share of less sophisticated retail investors rose—investors who might not be equipped or motivated to keep such a close eye on the prospects of the SPAC or to exercise their redemption rights if those prospects were undesirable.

C. SUMMING UP THE SPAC LITIGATION DELUGE

If pre-closing merger challenges produce immaterial disclosures in exchange for nuisance fees, there does not appear to be a plausible interpretation of the negative relationship between lawsuit probability and redemption rate that redeems these lawsuits. If these challenges target high-quality transactions, they are unhelpful. It seems highly unlikely that they are a common or logical substitute or complement for redemption. And if they target fraudulent transactions, they seem to be a failure under the very circumstances where they could, in theory, be most useful. Proponents of merger litigation may argue that these cases provide an opportunity for plaintiffs to force SPACs to improve or abandon their acquisitions and are therefore valuable. This potential indubitably exists and may represent the optimal result for investors, who could redeem their shares, or even, in the best case, benefit from a better deal without the injury of a bad transaction necessitating after-the-fact recompense. But I argue that merger objection lawsuits as they play out on the ground are not performing this role and are therefore undesirable, irrespective of whether they target fraudulent or high-quality deals.

Lawsuits brought after the merger are somewhat more difficult to characterize, in part because the vast majority have not been resolved. If low redemption rates are the product of misrepresentations, these lawsuits are likely meritorious. They also probably are effective deterrents of bad conduct; large class actions are among the more terrifying prospects to corporate management,[120] and perhaps even more so these days for SPACs, which are facing increasingly narrow D&O policies to insure against such lawsuits.[121] Class actions under Rule 10b-5 in particular are likely to be drawn-out affairs, and decreased insurance coverage may mean that the costs of such litigation may be more likely to fall on the defendant firm. But if the low redemption rates are the product of truthful disclosures and signal high-quality deals, the post-closing lawsuits challenging them may be

120. Myriam Gilles & Gary B. Friedman, *Exploding the Class Action Agency Costs Myth: The Social Utility of Entrepreneurial Lawyers*, 155 U. PA. L. REV. 103, 106 (2006) ("But does anyone seriously doubt that there is immense deterrent power in the contemporary class action? Executives tempted to lie about earnings are more concerned about [plaintiffs' lawyers] than they are about the Securities and Exchange Commission (SEC). Companies tempted to skirt fair credit reporting requirements are more concerned with ruinous liability at the hands of the class action bar than they are with the corrective measures and fines that might be meted out following a none-too-likely Federal Trade Commission (FTC) investigation." (footnotes omitted)).

121. Caroline Bullerjahn & Morgan Mordecai, *Limiting SPAC-Related Litigation Risk: Disclosure and Process Considerations*, HARV. L. SCH. FORUM ON CORP. GOVERNANCE (Mar. 14, 2021), https://corpgov.law.harvard.edu/2021/03/14/limiting-spac-related-litigation-risk-disclosure-and-process-considerations [https://perma.cc/9M8D-BXVX].

opportunistic. Plaintiffs' lawyers may be targeting these cases not because there is an indication of misconduct, but because a lower redemption rate means a larger class, more extensive purported damages, greater settlement pressure, and a higher potential payout.

Accordingly, it appears at this early stage that many of the lawsuits comprising the SPAC litigation deluge—the merger challenges brought before the merger—are accomplishing little other than a minimal payout for a few small plaintiffs' firms. Claims brought after the merger closes may effectively punish fraud. But it is also possible that even some of these lawsuits may be brought for opportunistic, rather than meritorious reasons. And if this is the case, they may be creating a significant cost for the transactions that appear to be of the highest quality. Fully disentangling these competing explanations—that SPAC-related litigation targets fraudulent transactions, or in fact targets quite good transactions—is a complex and perhaps impossible task. But there is at least a credible argument that much of this litigation may be failing to improve SPAC transactions and may be brought for reasons unrelated to SPAC quality.

V. THE BIGGER PICTURE: COMPARING SPAC MERGER LITIGATION TO SECTION 11 LITIGATION

SPACs are engineered specifically to avoid the expensive and time-consuming IPO process. More specifically, they are engineered, in some respects, specifically to avoid liability exposure under the securities laws, which is particularly stringent for IPOs.[122] Since the targets of SPACs go public through a merger instead of an IPO, they are governed by the regime for mergers instead of IPOs. In this section, I explore how, at this early stage, these different liability regimes stack up against each other.

A. PROBLEMS AVOIDED BY SPACS: SECURITIES ACT LIABILITY AND THE FORWARD-LOOKING STATEMENT SAFE HARBOR

There are two main reasons commonly cited for the reduced liability exposure faced by SPACs. These are liability under section 11 and liability for forward-looking statements.

The Securities Act of 1933 governs liability for primary offerings, including IPOs. A company issuing securities is strictly liable under section 11 of the Securities Act for material misstatements and omissions in its registration statement, the instrument by which it must register new shares

122. Press Release by John Coates, *supra* note 66.

for sale with the SEC.[123] The company's underwriters, officers, and directors are liable as well; although they may benefit from a "due diligence defense," in practice, this defense is available only under a very demanding standard.[124] Section 11 liability is virtually nonexistent in connection with SPACs. There are several reasons for this. First, the SPAC IPO occurs when the SPAC is a shell company and therefore has almost nothing in the way of operations or financials to disclose.[125] Second, SPACs could face section 11 liability in connection with the shares that they issue to target shareholders or PIPE investors in connection with the merger. However, once these shares mix in the market with shares issued in the IPO, it is very difficult to "trace" them to the registration statement of a particular offering. Such "tracing" is a requirement for the standing of a purported section 11 plaintiff, meaning that these cases are likely to be rare.[126]

The second reason commonly cited for going public via SPAC rather than via IPO is the safe harbor for forward-looking statements. The PSLRA allows issuers to make projections and forward-looking statements without fear of liability for such statements under the securities laws, as long as the statements are accompanied by meaningful cautionary language.[127] This safe harbor is unavailable in IPOs.[128] The ability to make forward-looking statements may be particularly valuable to pre-revenue SPAC targets, who do not yet have historical earnings with which to entice investors, or to firms in high-tech industries which require extensive start-up capital.[129] However, the demise of this advantage may be imminent;[130] regulators have hinted that

123. The other significant source of liability under the Securities Act, which is also more stringent than that of Rule 10b-5 is section 12(a)(2), which imposes liability for material misstatements and omissions in a prospectus. I do not focus on these claims because they are generally understood to require negligence, rather than strict liability, and because the content of a prospectus overlaps with that of a registration statement in most cases, they are frequently brought together. *See* THOMSON REUTERS, PRACTICAL LAW SECURITIES LITIGATION & WHITE COLLAR CRIME: SECURITIES ACT: SECTION 12(A)(2) ELEMENTS AND DEFENSES (2022) ("[P]laintiffs often file claims under Section 12(a)(2) together with Section 11 claims." (citations omitted)).

124. *See* Escott v. BarChris Constr. Corp., 283 F. Supp. 643, 684–701 (S.D.N.Y. 1968); *In Re* Worldcom, Inc., 346 F. Supp. 2d 628, 648 (S.D.N.Y. 2004).

125. *See* Klausner et al., *supra* note 4, at 271.

126. *Id.* Issuances in connection with the merger are not underwritten, meaning that underwriters escape liability for these issuances entirely. *Id.*

127. *See* 15 U.S.C. §§ 77z-2, 78u-5.

128. *Id.* § 77z-2 (a)(2)(d).

129. Daniele D'Alvia & Milos Vulanovic, *A Rethinking of U.S. Forward-Looking Statements in SPACs*, FORDHAM J. OF CORP. & FIN. L. (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/WF9Y-K5Z5].

130. The general rationale for eliminating the safe harbor for SPACs is to level the playing field between SPAC transactions and IPOs with respect to forward-looking statements. For a challenge to this rationale, see Amanda M. Rose, SPAC Mergers, IPOs, and the PSLRA's Safe Harbor: Unpacking Claims

the safe harbor may not apply to SPACs after all,[131] and the House of Representatives has released draft legislation explicitly eliminating the safe harbor for SPACs.[132]

B. MERGER LIABILITY FOR IPO LIABILITY: THE SPAC LAWSUIT SWAP

In going public via SPAC, firms essentially swap the IPO liability regime for the merger liability regime. What are the effects of this exchange? To examine how these lawsuits stack up against one another, I compare the merger objection lawsuits and unsued SPACs in my sample to a sample of IPOs from January 1, 2016, to July 31, 2021, matched with a sample of section 11 class actions from January 1, 2017, to June 31, 2021.[133] I gather my sample of section 11 class actions from the Stanford Securities Class Action Clearinghouse and the sample of non-SPAC IPOs from Zephyr.

Descriptive statistics are tabulated in Table 11. My total sample consists of 701 IPOs, 60 of which draw section 11 claims. Although the rate varies year over year (it spikes to over 17% in 2019, and the data for 2021 covers only the first half of the year, coming to nearly 3%), the average percentage of IPOs across the sample that draw a section 11 claim is 8.56%. This is far lower than the percentage of SPACs in my sample that drew merger objection claims during the same period (either under state corporate law or Rule 14a-9), which is 51.89%. Moreover, the average across the sample is understated since there are very few merger objection claims in the first three years of my sample; the average percentage in 2020 and 2021, when these lawsuits began to appear in earnest, is 67.69%.

The consequences of these lawsuits also appear to be dramatically different. The average settlement for section 11 lawsuits in my sample is roughly $4.5 million. In calculating this average, I include cases that were dismissed (where the settlement amount equals zero) and cases that are still ongoing (where the settlement amount is currently zero but may be significant when the case is resolved). This accounts to some degree for low

of Regulatory Arbitrage (Oct. 19, 2021) (unpublished manuscript), https://ssrn.com/abstract=3945975 [https://perma.cc/GN92-E9B3].

131. Press Release by John Coates, *supra* note 66 ("[T]he PSLRA safe harbor should not be available for any unknown private company introducing itself to the public markets . . . regardless of what structure or method it used to do so."). For further discussion, see John C. Coates, *supra* note 3, at 6–7.

132. Ran Ben-Tzur & Jay Pomerantz, *House Releases Draft Legislation Eliminating SPAC Safe Harbor for Forward-Looking Statements*, HARV. L. SCH. FORUM ON CORP. GOVERNANCE (June 7, 2021), https://corpgov.law.harvard.edu/2021/06/07/house-releases-draft-legislation-eliminating-spac-safe-harbor-for-forward-looking-statements [https://perma.cc/J472-NQQ7].

133. I build in a one-year lag between the IPO sample and the section 11 lawsuit sample because section 11 has a one-year statute of limitations. The timeframe for the lawsuits matches the one I use for SPAC-related litigation.

settlement values in the last few years of the sample. But the $4.5 million average, though likely substantially understated, is still much larger than the settlements that have so far been disclosed for merger objections in my sample, which average $200,000. Indeed, the likely reason that so few of such settlements are publicly available is that they are so small as to be immaterial to the issuers and therefore need not be disclosed.

There is also a divergence in the plaintiffs' firms that bring these cases. Section 11 lawsuits, across my sample, involve a top-tier plaintiffs' firm 63.3% of the time, and this number is relatively stable year over year (ranging from 60% to 69%). Top-tier plaintiffs' firms account for only 7.27% of the merger objection claims in my SPAC sample. Finally, the most commonly sued industries in the IPO sample are software and programming (21.67% of the sample) and biotechnology and drugs (11.67%). These are among the industries found in other studies to be particularly vulnerable to securities litigation.[134] By contrast, SPACs that draw lawsuits are generally not in these industries.

TABLE 11. Section 11 Lawsuit Descriptive Statistics

Year	*Section 11 Lawsuits*	*Mean Settlement**	*Percent Top Plaintiffs' Firms*[135]	*Total Non-SPAC IPOs*	*Percent Non-SPAC IPOs Sued Under Section 11*
2017	13	$15,600,000	69.23%	155	8.38%
2018	11	$6,445,455	63.64%	125	8.8%
2019	20	$813,750	60.0%	115	17.39%
2020	11	$0	63.64%	137	8.03%
2021	5 (as of June 31)	$0	60.0%	169 (as of July 31)	2.96%
Total	60	$4,571,841	63.3%	701	8.56%

Notes: *Mean settlement calculations include settlement values for lawsuits that were dismissed and lawsuits that are ongoing.

134. Skinner, *supra* note 56; Rogers & Stocken, *supra* note 56.

135. Top plaintiff firms are those in my sample that appear in The Legal 500 list for securities plaintiff litigation. LEGAL 500, *supra* note 54. Those appearing in my sample are Berman Tombacco, Bernstein Liebhard, Bernstein Litowitz Berger & Grossman, Cohen Milstein Sellers & Toll, Grant & Eisenhofer, Kessler Topaz, Labaton Sucharow, Pomerantz, and Robbins Geller Rudman & Dowd.

So, what can we make of all this? In terms of sheer litigation volume, SPACs appear to have fallen from the frying pan into the fire. Though designed in some respects specifically to avoid litigation under section 11, SPACs draw merger objection claims with dramatically greater frequency, and as previously discussed, the bulk of these claims are brought before the merger. However, insofar as information is available, these claims appear to settle for far lower amounts, meaning that for individual SPACs, the increased probability of a lawsuit may be outweighed by the apparently low probability of having to pay an expensive settlement. The majority of section 11 claims are brought by top-tier plaintiffs' law firms, which may indicate that they are stronger claims than the merger objections, which are brought by a handful of quite small entrepreneurs.

For IPOs, the policy choice has been to wield the heavy cudgel of virtually strict liability against those perceived to have the best knowledge about the newly public firm. This choice was made on the basis that firms new to the market, about which little is known, without any public history and potentially few profits for investors to assess, could be prime candidates for fraud. Investors in such firms have no source of information other than the firm itself, and Congress created the rigid liability provisions of the Securities Act to make that information as accurate as possible.[136] These provisions create the specter of extraordinary costs for those who violate them[137] and are thus commonly regarded as "well suited to deter misreporting."[138] Under the current legal framework, SPACs do not face this standard. Rule 10b-5 plaintiffs must plead specific allegations of, at the least, recklessness. Rule 14a-9 litigants must prove negligence to prevail,[139] which may be a more demanding task than it appears.[140] Under Delaware law,

136. This model is encountering increasing challenges as entrepreneurial firms without a history of profitability are commanding extraordinary valuations based on the possibility of future earnings. For a discussion of the role of investor protection in the face of these issues, see James J. Park, *Investor Protection in an Age of Entrepreneurship*, 13 HARV. BUS. L. REV. 107, 146 (2022).

137. *See* Donald C. Langevoort, *Deconstructing Section 11: Public Offering Liability in a Continuous Disclosure Environment*, 63 L. & CONTEMP. PROBS. 45, 45–47 (2000) (noting that "a sizable portion of the underwriters' spread is a liability risk premium, and lawyer-disseminated fear of liability casts a harsh shadow over the due diligence process" (footnotes omitted)).

138. Volker Laux & Phillip C. Stocken, *Managerial Reporting, Overoptimism, and Litigation Risk*, 53 J. ACCT. & ECON. 577, 579 (2012).

139. Press Release No. 51283, U.S. Sec. & Exch. Comm'n, Report of Investigation Pursuant to Section 21(a) of the Securities and Exchange Act of 1934 and Commission Statement on Potential Exchange Act Section 10(b) and Section 14(a) Liability (Mar. 1, 2005), https://www.sec.gov/litigation/investreport/34-51283.htm [https://perma.cc/8CY5-QXBT] ("Where the failure to make such disclosure is negligent, an issuer would violate Section 14(a) of the Exchange Act and Rule 14a-9 thereunder . . . .").

140. *See* Roger A. Cooper, James E. Langston, Mark E. McDonald & Charity E. Lee, *Rare Federal Court Decision Casts Doubt on Merger Disclosure Claims, but Will It Change Anything?*, CLEARY M&A

acquirers' challenges to mergers under state corporate law are usually reviewed under the deferential business judgment rule. Although there are good arguments that SPAC mergers, in view of potential management conflicts, should be reviewed under the more demanding "entire fairness" standard,[141] any of these standards is harder work for plaintiffs than the virtually strict liability of section 11.[142]

None of these concerns motivating the rigidity of section 11 liability are any less salient in SPACs, and given the conflicts commonly cited with respect to the SPAC form, they are arguably more intense. Yet, the merger litigation that replaces the Securities Act liability in the SPAC context appears to be significantly less costly to issuers—and indeed, that is probably one reason that the SPAC form is popular. It may be that merger litigation simply does not cost enough to induce SPACs to make the disclosures that would be optimal for investors in newly public firms.

But although most SPAC merger litigation may be insufficiently costly compared to Securities Act litigation, it is simultaneously too costly in that it is indiscriminate. Section 11 plaintiffs are constrained by unyielding standing rules[143] and generally have a fleeting one-year limitations period in which to make their claims.[144] These restrictions manifest in the relatively low number of IPOs that draw section 11 lawsuits—in my sample, less than

& CORP. GOVERNANCE WATCH (June 25, 2020), https://www.clearymawatch.com/2020/06/rare-federal-court-decision-casts-doubt-on-merger-disclosure-claims-but-will-it-change-anything [https://perma.cc/9XYB-AH9G] ("Unless a plaintiff can show that the proxy statement omitted a fact required to be disclosed by SEC regulations (which is often a tall task), the plaintiff must plead . . . with particularity, not merely with conclusory allegations—how the allegedly omitted fact renders the proxy statement disclosures materially misleading. But without knowing the facts that have been omitted—and because of the discovery stay imposed by the Private Securities Litigation Reform Act ("PSLRA")—plaintiffs will have difficulty obtaining such facts at the pleading stage . . . .").

141. *See* Klausner & Ohlrogge, *supra* note 39, at 12–13; *see also In re* MultiPlan Corp. S'holders Litig., 268 A.3d 784, 809 (Del. Ch. 2022); AP Servs. LLP v. Lobell, No. 651653/2012, 2015 WL 3858818, at *39–40 (N.Y. 2015) (declining to dismiss entire fairness claims against a SPAC under Delaware law where such a conflict was alleged); Ann Lipton, *Another SPAC Legal Development*, BUS. L. PROF BLOG (Aug. 7, 2021), https://lawprofessors.typepad.com/business_law/2021/08/another-spac-legal-development.html [https://perma.cc/73GT-H4N2].

142. It may be worth considering due diligence defenses for certain parties such as those available under section 11.

143. Plaintiffs must be able to "trace" their securities to the registration statement at issue, a task that is virtually impossible once the securities enter the secondary market. *See, e.g.*, *In re* Ariad Pharms Inc. Sec. Litig., 842 F.3d 744, 755 (1st Cir. 2016); Shapiro v. UJB Fin. Corp., 964 F.2d 272, 286 (3d Cir. 1992); *In re* WRT Energy Sec. Litig., No. 96 Civ. 3610, 1997 WL 576023, at *21 (S.D.N.Y. 1997); Gould v. Harris, 929 F. Supp. 353, 359 (C.D. Cal. 1996); *In re* AES Corp. Sec. Litig., 825 F. Supp. 578, 593 (S.D.N.Y. 1993).

144. 15 U.S.C. § 77m.

9%.[145] Although the limitations periods for much merger litigation are not much longer (often two or three years), standing rules are broader.[146] More importantly, the current regime for merger litigation generally allows for quick settlement for small fees without judicial oversight, meaning that no party involved has incentives to put the brakes on these lawsuits; plaintiffs may bring them irrespective of the merit of the case, defendants find it less expensive to pay than to challenge, and courts are not in a position to curtail the fees that are unwarranted or heighten those that are not.[147]

A high percentage of SPACs in the most recent years have drawn merger objection lawsuits. If these SPACs are fraudulent, $200,000 in fees is likely too low to create effective deterrence. If they are not, then many SPACs may be paying a "deal tax" that others have argued, in the standard merger context, is inappropriate.[148]

VI. POLICY IMPLICATIONS

Proposals for improving SPACs abound; academics,[149] regulatory agencies,[150] and even members of Congress[151] are busily gathering information and proposing reforms. Many of these proposals involve heightened disclosures of the various conflicts and relationships inherent in the structure of SPACs. These include, to name a few, sponsor compensation and the incentives sponsors have to close even a subpar deal, the stake that sponsors will have in the merged company, information about the diligence and negotiations that occurred during the merger process, and the probability and extent of dilution for shareholders who continue to hold their shares after the merger.

145. I note that the dramatically smaller percentage of IPOs drawing section 11 claims may also be a result of the higher scrutiny registration statements faced by issuers and underwriters because of the threat of strict liability.

146. Private plaintiffs are presumed to have standing under Rule 14a-9 if they are injured in connection with a proxy solicitation (no purchase or sale of securities is required). *See* THOMAS LEE HAZEN, TREATISE ON THE LAW OF SECURITIES REGULATION § 10:69 (2022). Shareholders have standing to challenge a merger if they owned stock at the time of the challenged transaction and throughout the litigation. If the lawsuit is derivative, they must either have demanded that the board initiate a lawsuit or adequately plead that the demand was futile. Harvey, *supra* note 113, at 1194.

147. See Cain et al., *Mootness Fees*, *supra* note 11, at 1783.

148. *Id.* at 1777.

149. *See, e.g.*, Klausner et al., *supra* note 4; Rodrigues & Stegemoller, *supra* note 4.

150. Dave Michaels, *SEC Weighs New Investor Protections for SPACs*, WALL ST. J. (May 26, 2021), https://www.wsj.com/articles/sec-weighs-new-investor-protections-for-spacs-11622052408 [https://perma.cc/88CM-PEC9].

151. Amrith Ramkumar, *Elizabeth Warren, Other Top Democrats Raise Concern About SPAC Incentives*, WALL ST. J. (Sept. 22, 2021), https://www.wsj.com/articles/elizabeth-warren-other-top-democrats-raise-concerns-about-spac-incentives-11632339583 [https://perma.cc/67B7-HPQW].

But perhaps these potential hazards are features, rather than bugs, of the SPAC structure. SPACs, say their proponents, "offer investors and targets a new set of financing opportunities that compete with later-stage venture capital, private equity, direct listings, and the traditional IPO process. They provide an infusion of capital to a broader universe of start-ups and other companies, fueling innovation and growth."[152] Of course, this breadth comes at a cost. SPACs are common for "firms [that] are speculative, have enormous capital requirements, and can provide only limited assurances on near-term revenue and viability."[153] Such investments are obviously risky. But one might assert that investors in SPACs understand this, or if they do not, they should. On this view, investors get to participate in these ostensibly high-reward deals in no small part *because* they lack the protections of a traditional IPO, and this bargain is a reasonable one that should be left intact.

The success of SPAC-related litigation depends on the camp into which one falls. Much of the SPAC litigation deluge is in fact composed of pre-closing merger challenges that probably generate little but low fees for plaintiffs' counsel. But if SPAC investors accept less information as part of a deliberate bargain for the opportunity to invest in ventures not normally available to them, then perhaps this litigation is functioning more or less as intended, and pre-closing merger challenges represent a minor deal tax[154] that all parties involved are willing to pay.

If, on the other hand, SPACs are not functioning as intended—if the informational goals of SPACs are analogous to those of standard IPOs, and shareholders have not knowingly bargained for them to be otherwise—then it appears that much SPAC-related litigation is not serving this goal. Rather, the merger challenges brought before the lawsuit are not promoting meaningful disclosure, and even a percentage of the smaller proportion of lawsuits brought after the merger may target transactions that can produce the biggest payout for plaintiffs' counsel, rather than targeting true misconduct. A natural conclusion of this line of thinking is that the system of private enforcement is currently ill-suited to correct the deficiencies of SPACs and that greater public intervention, such as government enforcement actions and more stringent regulation, may be necessary.

But this early sample of SPAC-related lawsuits has broader implications for the utility of shareholder litigation as a policing mechanism. The consolidation of the U.S. public equity markets has been the source of

152. Bazerman & Patel, *supra* note 1.
153. *Id.* at 105.
154. *See, e.g.*, Frankel, *supra* note 7.

commentary for some time.[155] The traditional IPO process has become the province of "large, late-stage companies."[156] Concurrently, small- and medium-cap companies—which have "[t]raditionally . . . delivered both higher risk and higher returns"[157]—have become far less accessible to the average investor.[158] The SPAC boom may be in part interpreted as a testament to retail investor appetite for such high-risk, high-return opportunities; retail investors eying the profits of venture capital and private equity moguls when the markets are rallying and money is flowing freely may well think, "Why not me?" Inaccessibility is a two-way street—smaller, growing firms that cannot access the liquidity of public markets could be limited in their opportunities for "economic growth, hiring, and wealth creation."[159]

While Congress and the SEC have undertaken efforts to make the traditional IPO process more inclusive,[160] the trend toward fewer, larger IPOs has proven persistent. It is thus not surprising—and is perhaps commendable—that private actors have experimented with alternative paths to the public markets. SPACs may not be the optimal result of these experiments. But in the absence of regulation that actually results in IPOs for more emerging, high-growth companies, such experimentation is likely to continue. Strong policing mechanisms for these experiments are necessary. Ex ante regulation, by its nature, is one or several steps behind such experiments, as SPACs aptly demonstrate. Regulation by agency enforcement is controversial, and even if it were not, agencies are resource-constrained and cannot catch everything. Shareholder litigation under broad, existing causes of action, such as Rule 10b-5, proxy fraud, and breach of fiduciary duty, constitutes a critical backup protection for investors in the face of private ordering experiments.

155. *See generally* Elisabeth de Fontenay, *The Deregulation of Private Capital and the Decline of the Public Company*, 68 HASTINGS L.J. 445 (2017); Andrew Ross Sorkin, *C.E.O.s Meet in Secret over the Sorry State of Public Companies*, N.Y. TIMES (July 21, 2016), https://www.nytimes.com/2016/07/21/business/dealbook/ceos-meet-in-secret-over-sorry-state-of-public-companies.html [https://perma.cc/52B4-86FV] ("[M]uch of the smart money in the United States is going—and staying—private . . . Publicly listed companies in the United States have become something of a dying breed.").

156. Spencer Israel, *The Number of Publicly Traded Companies in the US Is Shrinking—or Is It?*, MARKETWATCH (Oct. 30, 2020), https://www.marketwatch.com/story/the-number-of-companies-publicly-traded-in-the-us-is-shrinkingor-is-it-2020-10-30 [https://perma.cc/8XTT-FPP5].

157. Frank Partnoy, *The Death of the IPO*, ATLANTIC (Nov. 2018), https://www.theatlantic.com/magazine/archive/2018/11/private-inequity/570808 [https://perma.cc/M4MT-BY9R].

158. *Id.*

159. *Id.* (citation omitted).

160. *See, e.g.*, Statement, U.S. Sec. & Exch. Comm'n, Spotlight on Jumpstart Our Business Startups (JOBS) Act (Apr. 5, 2012), https://www.sec.gov/spotlight/jobs-act.shtml [https://perma.cc/SV5D-LUGW].

That some experiments, like SPACs, are designed to avoid certain types of liability (such as section 11) makes the efficacy of the remaining causes of action even more important. But if the SPAC-related litigation so far is anything to go by, it is unclear whether shareholder lawsuits are currently up to the job. Based on my sample, a very small subset of these lawsuits—post-closing merger challenges in the *Multiplan* mold—have resulted in standards that could improve a substantial shortcoming of the SPAC structure. The results of another 30% of these lawsuits—Rule 10b-5 claims—are as yet undetermined, but there are both meritorious and opportunistic explanations for these lawsuits, and the end results may lie somewhere in the middle. By far the largest bloc, comprising roughly half the claims in my sample, consists of pre-closing merger objections that are likely to perform little, if any, effective policing function.

This is most unfortunate, because in theory, these lawsuits could be among the most immediate and effective checks available against predatory structures innovated by private markets. The main advantage to merger objection claims is that they can be brought before a transaction closes, potentially saving shareholders from the consummation of a damaging deal. The supplemental disclosures issued in response to many merger objection claims could remedy prior misstatements or omissions and might force managers to do more comprehensive diligence or find better deals. The key advantage of a merger objection lawsuit is its immediacy; unlike most lawsuits, which can only be brought after the fact, merger challenges can directly affect the challenged transaction.[161]

161. This advantage is both more and less salient in the SPAC context. It is less salient in that where there is no fraud, it makes little sense for shareholders to sue when, if they dislike the transaction for any reason, they can redeem their shares. For a parallel discussion of the interaction of redemption rights with plaintiff's lawyer incentives in the mutual fund context, see John Morely & Quinn Curtis, *Taking Exit Rights Seriously: Why Governance and Fee Litigation Don't Work in Mutual Funds*, 120 YALE L. J. 84, 142 (2010). This remedy is more broadly available than the roughly analogous appraisal remedy available to target shareholders in other mergers under Delaware law, which bars appraisal for certain transactions and in general, for shareholders of corporations whose stock is listed on an exchange or held of record by more than two thousand holders. R. Franklin Balotti, Jesse A. Finkelstein, John Mark Zeberkiewicz & Blake Rohrbacher, 1 BALOTTI & FINKELSTEIN'S DELAWARE LAW OF CORPORATIONS & BUSINESS ORGANIZATIONS § 9.68 (4th ed. 2022). Shareholders electing to redeem their shares know exactly how much they will get, unlike shareholders seeking appraisal, who must rely in a judge's valuation. *Id.* Moreover, exercising the redemption right does not require the filing of a lawsuit. Favoring the redemption right, which is structurally similar to appraisal (but more shareholder-friendly in virtually every way) over such fiduciary class actions seems like common sense. *See* Charles Korsmo & Minor Myers, *Reforming Modern Appraisal Litigation*, 41 DEL. J. CORP. L. 279, 313 (2017) (finding that that appraisal actions are relatively rare and "associated with merits-related factors," and hence, "stand[] as the polar opposite of the system of fiduciary class actions"). If there is fraud, however, pre-closing merger lawsuits may actually be more valuable to SPAC investors than to investors in ordinary mergers because they could *enable* shareholders to exercise their redemption rights. It is difficult to dispute that in any

But based on my early sample of SPAC-related litigation, it is not at all clear that pre-closing merger objections are having this effect. They are so numerous and inexpensive that shareholders could easily be forgiven for not taking them seriously as a signal of real wrongdoing by the management. The disclosures they provide do not appear to induce shareholders to redeem. They do not appear to be related to the returns on the final deal. And the monetary penalties they exact are often too small even to be disclosed and likely would not deter unscrupulous SPAC managers from continuing to lie. All this aligns with the conclusions that have been swirling among scholars and judges in recent years; that "these suits are not being filed with the expectation of obtaining a meaningful recovery for the plaintiff class but rather in order to obtain a quick disclosure and mootness fee."[162]

This is a problem bigger than SPACs. In general,

> the time frames in which an M&A transaction must close usually discourage defendants from attempting to defeat pre-merger litigation on the merits, even when that litigation is abusive. And, even if settlement costs are minimal in comparison to the size of the M&A transaction, transaction costs associated with litigation end up being visited on shareholders, for no or little appreciable benefit.[163]

Correcting the broader environment that has allowed pre-closing merger litigation to become so dysfunctional is beyond the scope of this Article.[164] It is worth observing, however, that even if pre-closing merger objections have different significance in the SPAC context than in standard mergers, and even if SPACs are a phenomenon of the moment, pre-closing merger challenges are worth saving, if not for SPACs, then for future transactions and innovations. The first best solution for SPAC-related litigation, and indeed, for many other transactions, would be to save them.

merger, it is desirable to prevent shareholder votes for a transaction that are based on fraud. But in a standard merger challenge, even if some disclosure was fraudulent and even if the defendant firm issues a corrective disclosure before the merger, shareholders dissatisfied with the content of that disclosure will be stuck with the transaction if the majority votes for it. Not so for SPACs. The revelations induced by a pre-closing lawsuit may be more consequential to individual SPAC shareholders than to shareholders in ordinary mergers because SPAC shareholders are not captives to the board and the majority; if they do not like the information revealed by the lawsuit, they can get out if they want to. Accordingly, pre-closing merger lawsuits may be valuable where SPAC managers engage in fraud, potentially even more so to individual SPAC investors than to investors in more traditional transactions.

162. Cain et al., *Mootness Fees*, *supra* note 11, at 1783.

163. Rosenfeld v. Time Inc., No. 17-CV-9886, 2018 WL 4177938, at *4 (S.D.N.Y. Aug. 30, 2018).

164. A reasonable starting point, however, might be to consider extending the *Trulia* rule to other jurisdictions.

CONCLUSION

The litigation produced by the recent SPAC boom to date is intuitively odd: the likelihood of being sued is greater for SPACs whose shareholders elect to retain their shares, which suggests that they have greater confidence in the success of the merger. The likelihood that a de-SPAC transaction will generate a lawsuit does not, however, have to be related to the size of the deal, the experience of its managers, or virtually any other proxy for quality. This could mean that these lawsuits are, in fact, targeting fraudulent transactions, and the low redemption rates of these transactions reflect the fact that the shareholders have been lied to. Alternatively, it could mean that these lawsuits target low-redemption (and presumably higher quality) deals for some other reason, which may be opportunistic and unrelated to merit. Though these competing explanations are difficult to disentangle for the post-closing claims in my sample, I argue that the pre-closing merger cases in my sample do not appear to be meritorious, irrespective of whether they target fraudulent or non-fraudulent transactions. They do not appear to be an adequate substitute for section 11 liability, and if SPACs are in need of reform, private litigation may not be the optimal solution.