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Q2 2021 U.S. Legal & Regulatory Developments

The following is our summary of significant U.S. legal and regulatory developments during the second quarter of 2021 of interest to Canadian companies and their advisors.

1. The Impact of the Recent SEC Staff Statement on Accounting and Reporting Considerations for Warrants Issued by SPACs

On April 12, 2021, the Acting Director of the Division of Corporation Finance of the Securities and Exchange Commission (the "SEC") and the Acting SEC Chief Accountant published their Staff Statement on Accounting and Reporting Considerations for Warrants Issued by Special Purpose Acquisition Companies ("SPACs") (the "Staff Statement").

The Staff Statement states that if the warrants provide that the settlement amount may change based on the characteristics of its holder, the warrants should be classified as liabilities measured at fair value rather than being indexed to the entity's stock. Virtually all existing SPAC warrants provide that private warrants lose certain special features upon transfer and become fungible with the public warrants. This suggests that nearly all private warrants in existing SPAC structures must be reclassified as liabilities for accounting purposes.

The Staff Statement also indicates that if the warrants provide for net cash settlement upon the occurrence of an event outside of the entity's control, and if not all holders of the underlying equity securities would receive cash in such circumstances, then the warrant should be classified as a liability.

Pre-IPO SPACs may choose to revise the terms of their warrants to ensure that such warrants may be classified as equity, whereas parties to a de-SPAC transaction may wish to consider delaying closing to ensure that there is sufficient time to assess materiality and prepare revised financial statements, if necessary. Registrants should consult with their auditors and legal advisors to evaluate the terms of their warrants and determine whether reclassification is required.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3981076/the_impact_of_the_recent_sec_staff_statement_on_accounting_and_reporting_considerations_for_warrants_issued_by_spacs.pdf

For the SEC Staff Statement, please see:

- https://www.sec.gov/news/public-statement/accounting-reporting-warrants-issued-spacs

2. SEC Approves Amendments to NYSE Shareholder Approval Requirements

On April 2, 2021, the SEC approved the New York Stock Exchange's (the "NYSE") proposed amendments to its shareholder approval requirements applicable to issuances to directors, officers and substantial security holders ("Related Parties"), and to private placements in excess of 20% of a listed company's common stock by number of shares or by voting power. The NYSE rules are now largely consistent with the equivalent Nasdaq Marketplace Rules. The amended shareholder approval requirements provide companies with significantly greater flexibility to raise capital.

Issuances to Related Parties

The NYSE no longer requires shareholder approval for issuances to Related Parties in excess of 1% of a company's common stock if that issuance is made for cash at a price no less than the "Minimum Price" threshold.[1] Additionally, shareholder approval is no longer required for issuances to the subsidiaries, affiliates or other closely related persons of Related Parties. Shareholder approval is required in the case of issuances used to fund an acquisition where the Related Party has a 5% or greater, or a group of Related Parties collectively have a 10% or greater, direct or indirect interest in the company or assets to be acquired or the consideration to be paid.

Issuances in Excess of 20%

The NYSE no longer requires shareholder approval for private placements of more than 20% of a company's common stock (by number of shares or by voting power) so long as the issuance is made for cash and at a price no less than the Minimum Price, regardless of the number of investors participating in the offering. If the securities are to be issued in connection with the acquisition of the stock or assets of another company, and such securities together with other securities issued (or planned to be issued) in connection with the acquisition would equal or exceed 20% of the company's common stock (by number of shares or by voting power), then shareholder approval would be required.

Remaining Shareholder Approval Requirements

Issuances to Related Parties and issuances in excess of 20% remain subject to shareholder approval if required under any other applicable listing rule, including the equity compensation requirements of Section 303A.08 and the change of control requirements of Section 312.03(d). Related Party transactions, including issuances in excess of 20% which involves a Related Party, are subject to NYSE's Related Party transaction review requirements of Section 314.00 which requires the issuance to be pre-approved by the audit committee or another body of independent directors as consistent with the interests of the company and its shareholders.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980981/sec_approves_amendments_to_nyse_shareholder_approval_requirements.pdf

For our January 12, 2021 memorandum discussing the original proposed requirements, please see:

- https://www.paulweiss.com/media/3980756/update_on_nyse_shareholder_approval_requirements_waiver_extension_and_proposed_amendments.pdf

For the SEC order, please see:

- https://www.sec.gov/rules/sro/nyse/2021/34-91471.pdf

[1] "Minimum Price" means a price that is the lower of: (i) the Official Closing Price immediately preceding the signing of the binding agreement or (ii) the average Official Closing Price for the five trading days immediately preceding the signing of the binding agreement. The "Official Closing Price" of the issuer's common stock means the official closing price on the NYSE as reported to the Consolidated Tape immediately preceding the signing of a binding agreement to issue the securities.

For Amendment No. 1 to the Original Proposal, please see:

- https://www.nyse.com/publicdocs/nyse/markets/nyse/rule-filings/filings/2021/SR-NYSE-2020-85,%20Am.%201.pdf

For the Original Proposal, please see:

- https://www.sec.gov/rules/sro/nyse/2020/34-90803.pdf

3. SEC Approves Nasdaq Rule Change Permitting Primary Direct Floor Listings

On May 19, 2021, the SEC approved Nasdaq's proposed rule change to permit primary direct floor listings. This will permit companies to undertake an initial primary public offering and concurrent Nasdaq listing without the use of underwriters to market the shares (a "Direct Listing with a Capital Raise"). Prior to the rule change, direct listings were available only for secondary offerings by existing shareholders. The rule change allows for primary direct listings to occur alone or together with a secondary direct listing. Primary direct floor listings have been permitted on the NYSE since December 2020.

Listing Requirements

Companies undertaking a Direct Listing with a Capital Raise will be deemed to meet the applicable Market Value of Unrestricted Publicly Held Shares requirement (as defined in the proposed rule change) if the aggregate market value of unrestricted publicly held shares immediately prior to listing, together with the market value of shares the company sells in the opening auction, total at least $110 million (or $100 million, if the company has stockholders' equity of at least $110 million), with such market value calculated using a price per share equal to the price that is equal to the lowest price of the range disclosed by the issuer in its effective registration statement.

The company listing via a Direct Listing with a Capital Raise will be required to comply with all other initial listing requirements, namely, having the applicable minimum number of shareholders per Nasdaq Listing Rule 5315(f)(1), at least 1,250,000 unrestricted publicly held shares outstanding at the time of initial listing, and a price per share of at least $4.00 at the time of initial listing.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3981117/sec_approves_nasdaq_rule_change_permitting_primary_direct_floor_listings.pdf

For our September 18, 2020 memorandum discussing Nasdaq's original proposal, please see:

- https://www.paulweiss.com/media/3980479/sec_publishes_nasdaqs_proposal_for_direct_listings_with_a_capital_raise.pdf

For Amendment No. 2 to the Original Proposal, which completely superseded and replaced Nasdaq's original proposal, please see:

- https://listingcenter.nasdaq.com/assets/rulebook/nasdaq/filings/SR-NASDAQ-2020-057_Amendment_2.pdf

For the Original Proposal as amended by Amendment No. 1, please see:

- https://listingcenter.nasdaq.com/assets/rulebook/nasdaq/filings/SR-NASDAQ-2020-057.pdf

SEC Poised to Consider ESG Disclosures
After receiving hundreds of submissions, the SEC closed its period of public comment on the topic of climate-change disclosures on June 13, 2021. The comments reflected a range of views, with some parties suggesting that the SEC should or must limit itself to financially material disclosures, and others raising First Amendment concerns. As for materiality itself, some businesses supported the materiality of climate-related disclosures, while others encouraged the SEC to require company-specific assessments rather than a generic approach.

Environmental, social and governance ("ESG") factors have received heightened attention since the inauguration of President Biden. On March 4, 2021, the SEC announced the creation of a Climate and ESG Task Force in its Division of Enforcement. On May 20, 2021, President Biden issued an Executive Order on Climate-Related Financial Risk that called on the federal government to take concrete steps to mitigate the physical and transitional risks of climate change. Among other steps, the Executive Order directed the Secretary of the Treasury to work with the Financial Stability Oversight Council to review climate-related disclosures. On March 15, 2021, then-Acting-Chair Commissioner Lee called for public input on disclosures related to climate change, and over 320 individual comments were submitted.

As the SEC sharpens its focus on climate- and ESG-related disclosures, and in the wake of the end of the public comment period, the prospect of additional rulemaking continues to increase, and SEC staff has indicated that it could occur soon.

For the full text of our client alert, please see:

- https://www.paulweiss.com/media/3981198/sec_poised_to_consider_esg_disclosures.pdf

For our March 2021 client alert discussing the Climate and ESG Task Force in the Division of Enforcement and the broader regulatory environment, please see:

- https://www.paulweiss.com/media/3980479/sec_publishes_nasdaqs_proposal_for_direct_listings_with_a_capital_raise.pdf

4. Regulatory Focus on Vertical Mergers May Impact Investor Exit Strategy Planning

Antitrust enforcers are expected to increase their scrutiny of vertical mergers, being mergers involving companies at different levels of the supply chain. Most vertical mergers will likely not present competitive concerns and will not attract lengthy agency investigation. However, for certain transactions at the margins, if a more aggressive stance toward vertical merger enforcement becomes the majority view at the Federal Trade Commission (the "FTC"), we can expect challenges to or extended review of some transactions that may have previously avoided regulatory scrutiny or may have been allowed to proceed with modifications or conditions.

This could have important consequences for private equity sponsor exit strategies, which often involve vertical acquisitions of earlier-stage companies by more established companies. Investors and their advisors should weigh the regulatory risks of various exit options, as these risks may impact a potential transaction's timing and overall chance of success. Additionally, an increased focus on vertical mergers in the United States may have consequences for regulators in other jurisdictions: those non-U.S. agencies that are already skeptical of vertical deals may become even more skeptical if the regulatory climate in the United States becomes more aggressive.

The current FTC vertical merger challenge of Illumina, Inc.'s proposed acquisition of Grail, Inc. serves as an important reminder that investors planning or contemplating potential exit strategies must take into account antitrust considerations for vertical mergers. The challenge, taken together with the court of appeals' opinion in the U.S. Department of Justice's lawsuit seeking to enjoin AT&T's acquisition of Time Warner, may inform the extent to which merging parties will be able to proactively undertake unilateral commitments as a viable and reliable strategy to address perceived risks associated with vertical integration.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3981034/regulatory_focus_on_vertical_mergers_may_impact_investor_exit_strategy_planning.pdf

For the FTC announcement of its challenge against Illumina, Inc.'s proposed acquisition of Grail, Inc., see:

- https://www.ftc.gov/news-events/press-releases/2021/03/ftc-challenges-illuminas-proposed-acquisition-cancer-detection

For the FTC's complaint against Illumina, see:

- https://www.ftc.gov/system/files/documents/cases/redacted_administrative_part_3_complaint_redacted.pdf

5. SEC Staff Suspends Enforcement of Proxy Voting Advice Guidance and Rule Changes Pending Ongoing Review

On June 1, 2021, the Staff of the SEC's Division of Corporation Finance (the "CorpFin Staff") announced its intent to forego enforcement of proxy rules regarding the treatment of proxy voting advice as proxy solicitations. In 2019, the SEC issued guidance on, and in 2020, amended, these proxy rules.

Institutional Shareholder Services ("ISS") is challenging the 2019 guidance and 2020 amendments on the grounds that they exceed the SEC's statutory authority, are procedurally improper, are "arbitrary and capricious" and violate the First Amendment.

While the CorpFin Staff considers whether to revisit the 2019 guidance and 2020 amendment and issue further regulatory action, it will not recommend enforcement actions. If any new regulatory action includes the exemption conditions and compliance date set forth in the 2020 amendments, the CorpFin Staff will not recommend any enforcement based on those conditions for a reasonable period of time after the resumption of the ISS challenge.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3981156/sec_staff_suspends_enforcement_of_proxy_voting_advice_guidance_and_rule_changes_pending_ongoing_review.pdf

For the 2019 guidance included in the SEC Statement on Compliance, please see:

- https://www.sec.gov/news/public-statement/corp-fin-proxy-rules-2021-06-01?utm_medium=email&utm_source=govdelivery

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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