

CAQ International Practices Task Force (IPTF)
November 20, 2007 - Joint Meeting with SEC Staff

Discussion Document B

Topic: Financial Statement Requirements in Form 8-K after a Foreign Company Completes a Reverse Acquisition of a U.S. Public Shell Company

Background:

- A foreign company is completing a reverse acquisition of a U.S. domestic registrant shell company.
- To effect the reverse acquisition, a Form S-4 was filed with statements of the foreign company (accounting acquirer) in home-country GAAP reconciled to U.S. GAAP in compliance with Item 18.
- A Form 8-K will be filed upon consummation of the transaction.

Issue:

Related to the Form 8-K that will be filed upon consummation of the merger in the above fact pattern, questions that often arise include:

1. Within how many days after the consummation of the merger is the Form 8-K due?
2. What GAAP should be used to prepare the financial statements of the foreign company (accounting acquirer) included in the Form 8-K?

Discussion

To address these questions, issuers often refer to guidance in the SEC Staff Training Manual and the SEC Staff's outline (that is, the International Financial Reporting and Disclosure Issues in the Division of Corporate Finance). Relevant excerpts (emphasis added) from these publications are as follows:

SEC Staff Training Manual, Exhibit B, Reverse Acquisitions.

Form 8-K

1. ***A Form 8-K should be filed not later than 15 days after the consummation of the reverse acquisition. That Form 8-K should note under the appropriate Form 8-K item number any intended change in independent accountants and changes in fiscal year end from that used by the registrant prior to the acquisition. Most typically, registrants adopt the fiscal year and auditor of the accounting acquirer, but that is not necessary.***
2. ***The Form 8-K reporting the acquisition should contain financial statements of the accounting acquirer (the legal acquiree). Those financial statements thereafter***

become the financial statements of the registrant pursuant to GAAP. Audited financial statements of the accounting acquirer for the three most recently completed fiscal years should be included; or two years, if the registrant was eligible to use S-B forms and effected that election in its initial filing in the fiscal year in which the merger occurred.

3. *Unaudited interim financial statements of the accounting acquirer for any interim period and the comparable prior year period, and pro forma information depicting the effects of the acquisition, should be included in the Form 8-K. If the financial statements of the accounting acquirer are not available, the registrant has up to 75 days from the date the acquisition was consummated to furnish the required information.*

SEC Staff Training Manual, Topic 6 (Foreign Private Issuers and Foreign Businesses), Chapter III (Requirement for Reconciliation to US GAAP), Item A.4

4. *"Backdoor" listings by foreign companies*
 - a) *Foreign companies sometimes obtain a "backdoor" listing through a reverse acquisition with a U.S. public shell. Even though substantially all of the operations are conducted outside of the U.S., the registrant would not be considered a foreign private issuer.*
 - b) ***To facilitate timely reporting, the staff would not object if the financial statements included in the Form 8-K are prepared using a foreign GAAP, provided a reconciliation to U.S. GAAP that complies with Item 18 of Form 20-F is provided.***
 - c) *The first Form 10-K and any registration statement should include financial statements prepared using U. S. GAAP for all periods presented, including those prior to the reverse acquisition. Financial statements in a foreign GAAP reconciled to U.S. GAAP would not be acceptable.*

SEC – International Financial Reporting and Disclosure Issues in the Division of Corporate Finance, (November 1, 2004) section VI. – Issues Encountered in Reconciliations to US GAAP/Business Combinations/Financial Statement Requirement after a Reverse Acquisition.

*A number of foreign companies have obtained a listing in the US by merging into a nonoperating US public shell company whose securities are already registered with the Commission. The transaction is typically accounted for as a "reverse recapitalization." Notwithstanding that substantially all of the registrant's operations after the merger will be conducted outside of the US, the registrant is not a foreign private issuer and must comply with the rules applicable to US public companies. **Accordingly, the registrant must file a Form 8-K containing financial statements of the foreign company within 75 days of the merger. To facilitate the initial filing of the foreign company's statements, the staff will not object if the financial statements included in the 8-K are prepared in accordance with a foreign GAAP, but reconciled to US GAAP in accordance with Item 18 of Form 20-F.** However, the first Form 10-K following the merger, and any registration statement, should include financial statements prepared in accordance with*

US GAAP for all periods presented, including those periods prior to consummation of the reverse recapitalization. Financial statements in a foreign GAAP reconciled to US GAAP would not be acceptable.

SEC Rule Release 33-8587

In July 2005, the SEC published its final rule, *Use of Form S-8, Form 8-K, and Form 20-F by Shell Companies* (“Rule Release 33-8587”). The new rule requires substantially more disclosures, on a timely basis, when a public shell company ceases to be a shell company (e.g., the acquisition of more than nominal assets; the acquisition of an operating business, including a reverse merger or back-door registration). In addition, the rule prohibits a public shell company from using Form S-8, and prohibits a former public shell company from using Form S-8 until 60 days after it files the specified disclosures. These rules target regulatory problems that the SEC had identified where shell companies have been used as vehicles to commit fraud and abuse their regulatory processes.

Pursuant to these rules, the SEC requires that the surviving entity file its report on Form 8-K within four business days after completion of the transaction that it is required to report. The SEC believes the timeframe is appropriate because shell companies and their counsel control the pace and timing of these transactions. Given the concerns unique to shell company transactions, the SEC believes shell companies should complete a transaction that is required to be reported only when they can timely provide investors with adequate information to make informed investment decisions.

Under the new rules, the financial statements of the accounting acquirer of a shell company must be filed within four business days and must be equivalent to that required in a Form 10 Exchange Act registration.

Discussion

Issue 1 – With respect to a foreign company obtaining a “backdoor” listing through a reverse acquisition of U.S. public shell company, the new rules shortened the time period to file the 8-K (i.e., 4 days). However, a preparer relying on the guidance in the SEC – International Financial Reporting and Disclosure Issues in the Division of Corporate Finance, (November 1, 2004) could inappropriately interpret that guidance to provide 75 days from the date of the merger to file the financial statements by amendment to the 8-K. Therefore, to some, it is unclear as to whether the accommodation to timing is still granted by the SEC Staff.

Issue 2 – Rule Release 33-8587 is silent with respect to the acceptability of the foreign company (accounting acquirer) filing home-country GAAP reconciled to U.S. GAAP in the 8-K. Some believe that considering the SEC’s intent with respect to Rule Release 33-8587 and the preparer and counsel control of timing of the transaction that the accommodation to provide home-country reconciled to U.S. GAAP should be discontinued. Others are not troubled by the foreign company (accounting acquirer)

continuing to be able to use home-country GAAP reconciled to U.S. GAAP in the Form 8-K.

With respect to both issues, the Task Force believes that the SEC Staff should update the publications mentioned above so as to avoid confusion in practice amongst preparers and their counsels.

Proposed Task Force Recommendation:

Considering the SEC's intent with respect to Rule Release 33-8587 and that the financial statements of the accounting acquirer (i.e., foreign company) become the primary financial statements of the registrant and will have to be prepared in accordance with U.S. GAAP, the Task Force recommends that the SEC Staff update the SEC – International Financial Reporting and Disclosure Issues in the Division of Corporate Finance, (November 1, 2004) mentioned above as follows:

- The registrant must file a Form 8-K containing financial statements of the foreign company within 4 business days of the merger.
- The financial statements of the foreign company (accounting acquirer) included in the 8-K should be prepared in accordance with a U.S. GAAP.

Furthermore, the Task Force believes these actions will protect investors by deterring fraud and abuse in the U.S. securities markets through the use of reporting shell companies.

SEC Staff Response:

The staff agrees with the Task Force's view.