

SEC Regulations Committee
April 17, 2007 - Joint Meeting with SEC Staff
SEC Offices – Washington DC

Discussion Document B

Topic: Application of FAS 158 in Connection with an Initial Public Equity Offering

Issue: Should a private company that undertakes an IPO in 2007 reflect the adoption of FAS 158 as if that company had always been a public company?

Background: Companies with publicly-traded equity securities must adopt the recognition provisions of FAS 158 beginning with fiscal years ending after December 15, 2006. Companies that do not have publicly-traded equity securities must adopt the recognition provisions of FAS 158 no later than fiscal years ending after June 15, 2007. FAS 158, paragraph 16 states:

An employer shall apply the recognition provisions of this Statement as of the end of the fiscal year of initial application. Retrospective application is not permitted...

Consider the following example:

Company X, a private company with a calendar year-end is preparing an S-1 in June 2007 for an IPO. The S-1 includes audited financial statements as of December 31, 2006 and 2005 and for each of the three years in the period ended December 31, 2006 and unaudited financial statements as of March 31, 2007 and for the three-month periods ended March 31, 2007 and 2006. Company X had previously submitted its December 31, 2006 financial statements to its bank and its shareholders under "private company GAAP" (e.g., it had not adopted FAS 158 in those financial statements).

Question 1: When preparing the IPO Form S-1, is Company X required to reflect the adoption of the recognition provisions of FAS 158 as of December 31, 2006 (i.e., as if it had always been a public company)?

View A: When preparing the IPO Form S-1, Company X must revise its December 31, 2006 financial statements to reflect the adoption of the recognition provisions of FAS 158 to the same extent as if Company X had always had publicly-traded equity securities. Additionally, Company X must also apply the recognition provisions of FAS 158 in the March 31, 2007 interim financial statements.

View B: Company X must reflect the adoption of the recognition provisions of FAS 158 in Q2 of 2007. This would give weight to the fact that the company was still private during the periods covered by the financial statement and would take into account the "no-retrospective application" concept included in FAS 158.

View C: Company X must reflect the adoption of the recognition provisions of FAS 158 in Q1 of 2007. This would reflect the "no-retrospective application" concept included in FAS 158.

View D: Company X should not reflect the adoption of the recognition provisions of FAS 158 until its 2007 Form 10-K.

Committee Recommendation: The Committee supports View A. The Committee discussed a similar issue with the Staff at the April 2004 meeting (relating to adoption of FAS 150). Similar to FAS 150 (and certain other accounting standards), FAS 158 has accounting treatment alternatives for public and non-public entities. An entity is generally no longer eligible for the non-public company treatment alternatives when it is in the process of

becoming a public entity. Such entities must comply with public company treatment alternatives in the standard as of the date that all public companies were required to adopt the standard, even if that requires a company that is in the process of filing an IPO to restate prior period financial statements. This approach is consistent with the staff's past practice for adoption of new standards with different transition provisions for public and non-public entities.

SEC Staff Response: The Staff supports View A.

Question 2: Would the answer to Question 1 be different if Company X was a debt-only issuer prior to commencing its common equity IPO and had been filing Exchange Act reports with the Commission (because of the outstanding registered debt) since 2003?

View A: Yes. Company X was not required to follow the recognition and measurement provisions of FAS 158 in connection with its 2006 Form 10-K (because Company X did not meet FAS 158's definition of a company with publicly traded equity). If Company X did not early adopt the recognition provisions of FAS 158 in connection with its 2006 10-K, then it would not be required to restate those financial statements in connection with the Form S-1. Since the recognition provisions of FAS 158 can only be adopted as of a company's fiscal year-end, Company X will not be required to adopt FAS 158 until its fiscal year ended December 31, 2007.

View B: No. The answer is the same as the answer to Question 1. Although Company X would not be required to file amendments to its 2006 Form 10-K and March 31, 2007 Form 10-Q, it would be required to retrospectively apply the recognition provisions of FAS 158 in the December 31, 2006 and March 31, 2007 financial statements included in the Form S-1 on the same basis as if they had always had publicly-traded equity.

Committee Recommendation: The Committee supports View A. Consistent with a follow-up question addressed with respect to the adoption of FAS 150 (see Discussion Document G from the April 2004 meeting), the Committee believes that the prior public reporting history of Company X should be respected. Company X should not be required to restate its previously filed financial statements to retrospectively apply the recognition provisions of FAS 158. The Committee notes that FAS 158 prohibits retrospective application. Company X could elect to restate its previously filed financial statements (but not for periods that precede the initial effective date of FAS 158). The Committee also notes that Company X's prior Exchange Act reports would include the disclosures required by SAB 74 and paragraph 14 of FAS 158, as appropriate. Those disclosures should also appear in the financial statements included in the Form S-1.

SEC Staff Response: The staff would not object to View A. Consistent with the Committee recommendation, the staff indicated that it would not object if such an issuer elects to restate its financial statements for the first fiscal year ending after December 15, 2006 (and any subsequent interim periods provided in the registration statement) to reflect the adoption of FAS 158, with clear disclosure of such restatement(s).

