



CAQ Alert #2007-39 – August 2, 2007

DEAR CENTER MEMBERS

Time-Sensitive Issues from SEC Regulations Committee Meeting with SEC- July 2007

On July 10, 2007, the Center's SEC Regulations Committee met with the SEC staff to discuss emerging technical accounting and reporting issues relating to SEC rules and regulations. The highlights from this meeting will be posted to the [SEC Regulations Committee Web Page](#) when they are finalized. The following is a summary of the ***time-sensitive issues*** discussed at the meeting that might be of interest to you.

Risk Factors Related to the Financial Reporting Process

Sometimes registrants disclose risk factors identifying potential risks that the registrant might be required to restate or make other changes to financial statements. These risk factors discuss the complexities of the accounting standards, explain that they can be interpreted or applied differently, either by the SEC staff or by successor auditors (when there has been a change in auditors), and communicate that such differences in interpretation or application could cause a restatement of the registrant's financial statements. The Committee solicited the SEC staff's views as to when such risk factor disclosures might be appropriate. The SEC staff expressed concern that such disclosures could be an attempt to dilute the responsibility that the registrant takes for its financial statements. The SEC staff also stated that a risk factor would not satisfy the specificity required by SK Item 503(c) if the registrant merely identifies the complexity of financial reporting and the generic risk of a subsequent financial restatement. However, the SEC staff noted that, as part of its review of a specific filing, it will evaluate specific risk factors based on a registrant's specific facts and circumstances.

Reporting on Internal Controls in a Reverse Merger and the December 2006 Release

In light of the December 2006 amendments that provide an "IPO accommodation" by deferring Section 404 reporting by a new public company until its second SEC annual report, the Committee asked the SEC staff for its views on whether this accommodation also would apply in a reverse merger when the accounting acquirer was not a public company. The SEC staff noted that it continues to address the reporting requirements of a reverse merger on a facts and circumstances basis. Accordingly, a registrant with this fact pattern is encouraged to consult with the legal staff in the Division of Corporation Finance's Office of the Chief Counsel to determine its Section 404 reporting requirements.

Executive Compensation Disclosures

The SEC staff stated that it is performing reviews of 2007 proxy filings for compliance with the new executive compensation disclosure rules. The SEC staff has not issued any comment letters on the proxy reviews yet, but has issued comment letters on the executive compensation disclosures in transactional filings. The SEC staff noted that although registrants have generally been doing a good job in adhering to the new rules, there have been a number of recurring observations that have been noted in comment letters:

- The CD&A could provide better analysis of executive compensation decisions.
- If registrants have an adequate basis for omitting incentive plan performance targets, they should provide the alternate disclosure regarding the relative likelihood that those performance targets will be met.
- Descriptions of incentive plan performance targets should be specific.
- Regardless of the terminology used, “benchmarking” executive compensation should be accompanied by an identification of the other companies that were used for benchmarking purposes.
- In disclosing executive compensation decisions, registrants should provide a clear description about the respective roles and responsibilities of the CEO, compensation consultants and the compensation committee in the decision making process.

The SEC staff is considering what guidance, if any, to issue addressing the results of the compliance reviews.

Emerging Practice Issues Included in Discussion Documents

The following emerging practice issues were addressed at the July 10, 2007 meeting with the SEC staff and discussion documents have been posted to the Center’s website at the respective URLs:

- A. [Reporting Requirements of Rule 4-08\(g\) of Regulation S-X for Periods in which the Investee is Less than 10% Significant](#)
- B. [When Rule 3-05 Financial Statements Must be Provided in Registration Statements Covering Secondary Offerings](#)
- C. [Applying Rule 3-09 of Regulation S-X to an Equity Method Investee in the Real Estate Industry](#)
- D. [When Stock Based Executive Compensation That Is Capitalized or Deferred Should Be Reported In The Summary Compensation Table](#)

Stay Informed

As a member of the Center, your firm will receive periodic updates on important developments related to the PCAOB and the SEC, as well as the activities of the Center, particularly with respect to the submission of comment letters on PCAOB and SEC proposals. To stay abreast of these and other relevant events in public company audit practice, please visit the Center Web site at theCAQ.aicpa.org. Also, we welcome any suggestions or questions - please send them by email at center@theCAQ.org.

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