CAQ SEC Regulations Committee
June 27, 2012 - Joint Meeting with SEC Staff
SEC Offices – Washington DC

HIGHLIGHTS

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In addition, these highlights are not authoritative positions or interpretations issued by the SEC or its staff. The highlights were not transcribed by the SEC and have not been considered or acted upon by the SEC or its staff. Accordingly, these highlights do not constitute an official statement of the views of the Commission or of the staff of the Commission.

As available on this website, Highlights of Joint Meetings of the SEC Regulations Committee and its International Practices Task Force (IPTF) and the SEC staff are not updated for the subsequent issuance of technical pronouncements or positions taken by the SEC staff, nor are they deleted when they are superseded by the issuance of subsequent highlights or authoritative accounting or auditing literature. As a result, the information, commentary or guidance contained herein may not be current or accurate and the CAQ is under no obligation to update such information. Readers are therefore urged to refer to current authoritative or source material.

I. ATTENDANCE

A. SEC Regulations Committee

Melanie Dolan, Chair
Steve Meisel, Vice Chair
Jim Brendel
Jack Ciesielski
Brad Davidson
Christine Davine
Jack Day
Tom Elder

Jeff Lenz
Scott Pohlman
Michelle Stillman

B. Securities and Exchange Commission

Division of Corporation Finance (Division)

Craig Olinger, Acting Chief Accountant
Nili Shah, Deputy Chief Accountant
Angela Crane, Associate Chief Accountant
Jill Davis, Associate Chief Accountant
Louise Dorsey, Associate Chief Accountant
Todd Hardiman, Associate Chief Accountant
Joel Levine, Associate Chief Accountant
Ryan Milne, Associate Chief Accountant
Kyle Moffatt, Associate Chief Accountant
Leslie Overton, Associate Chief Accountant
Mark Shannon, Associate Chief Accountant
Michael Stehlik, Assistant Chief Accountant
Mark Green, Senior Special Counsel
Jennifer Zepralka, Senior Special Counsel

C. Center for Audit Quality

Annette Schumacher Barr

D. Guests

Rob Skubic, KPMG
John May, PwC
Scott Ruggiero, Grant Thornton
Tu Hu, CAQ
Mary Higgins, EY

II. DIVISION OF CORPORATION FINANCE PERSONNEL AND ORGANIZATIONAL UPDATE

Craig Olinger indicated that there had not been any notable personnel or organizational changes in the Division of Corporation Finance since the last SEC Regulations Committee meeting in March 2012.

III. CURRENT FINANCIAL REPORTING MATTERS

A. Classification of Cash and Short Term Investments Held in Jurisdictions Where the Indefinite Reinvestment Assertion Has Been Made

The Committee discussed with the SEC staff recent limited instances in which the SEC staff had asked registrants about the balance sheet classification of cash and short term investments held in jurisdictions where the indefinite reinvestment assertion has been made.

Nili Shah indicated that the SEC staff's view is that the mere holding of cash or short term investments in a jurisdiction where the indefinite reinvestment assertion has been made would not require classification as restricted cash in the balance sheet.

B. Recent SEC Staff Remarks Relating to Non-GAAP Financial Measures for Pension Accounting

Ms. Shah summarized the recent public comments made by Jim Kroeker, Chief Accountant of the SEC at that time, with respect to the SEC staff's focus on pension-related (including other post-retirement employee benefits) non-GAAP financial measures. Ms. Shah indicated that Mr. Kroeker's comments highlighted the SEC staff's observation that some companies that recently changed their method of accounting for pension plan investments (e.g., immediately recognizing in the income statement gains and losses attributable to the change in the fair value of investments held in defined benefit plans) have presented non-GAAP financial measures that remove the actual gain or loss from the performance measure and include an expected long-term rate of return. Ms. Shah noted that this type of measure has the potential to create investor confusion absent sufficient context regarding the nature of the adjustment.

Ms. Shah also noted that the SEC staff has observed other instances of unclear disclosures by registrants in the presentation of non-GAAP financial measures that remove a portion of pension expenses.

Regardless of the registrant's policy for recognizing actuarial gains and losses in its GAAP financial statements, the SEC staff may comment on non-GAAP disclosures that remove pension-related expenses in the following circumstances:

- Disclosures do not clearly describe what the adjustment represents (e.g., the adjustment removes the amount of actuarial gain / loss immediately recognized in earnings, the adjustment removes all non-service related pension costs, or the adjustment removes all pension expense in excess of cash contributions).

- Disclosures do not provide quantitative context for the actual and expected returns on plan assets.

- Adjustment is described as "non-cash," even though the pension liability is ultimately settled in cash, or "non-recurring," even though the adjustment is reasonably likely to recur within two years or there was a similar adjustment within the prior two years.

- Disclosures do not provide a reasonable basis as to why management believes the non-GAAP measure provides useful information to investors.

C. Pro Forma Adjustments for Items with "Continuing Impact"

S-X Rule 11-02(b)(6) requires that a pro forma income statement include only adjustments that give effect to events that are (i) directly attributable to the transaction, (ii) expected to have a "continuing impact" on the company, and (iii) factually supportable.

Ryan Milne indicated that the SEC staff has modified the view it expressed at the December 2011 AICPA National Conference on Current SEC and PCAOB Developments with respect to what constitutes "continuing impact." At that time, the SEC staff communicated the view that items have a continuing impact if they are expected to impact operations or recur for a period greater than 12 months from the date of the initial occurrence. However, in light of certain types of pro forma adjustments that were recently considered, the SEC staff now views items to have a continuing impact if they are not "one time." Examples of items which may be considered to have a continuing impact under this updated view include interest expense for a bridge loan that may be incurred for a period of less than twelve months or amortization of an acquired intangible asset with a short life (e.g., six months).

Todd Hardiman indicated that this updated view does not affect the SEC staff's views with respect to the pro forma impact of transaction expenses incurred in connection with a business combination. The SEC staff's guidance set forth in FRM 3250 is still applicable.

D. Revision to Previously Filed Financial Statements In Connection With a New or Amended Registration Statement (other than Form S-8)

Ms. Shah shared the SEC staff's views about whether a registrant should revise its previously filed historical annual financial statements in connection with a new or amended registration statement (other than Form S-8) when a new accounting standard or another accounting item (e.g., discontinued operations) has been retrospectively reflected in the registrant's filed interim

financial statements. The guidance with respect to Form S-8 is set forth in the Note to Section 13100 in the FRM.

The SEC staff indicated that, in general, if a registrant adopts a new accounting standard retrospectively (or applies other changes required by GAAP retrospectively) in its interim financial statements and the registrant intends to reflect the retrospective revision in prior year comparative annual financial statements included in its next annual report, the SEC staff would expect the registrant to file revised annual financial statements prior to filing a new or amended registration statement (other than Form S-8) if the impact on those prior period financial statements is material. The SEC staff noted that if a registrant does not file revised financial statements then there will be an inconsistency between the basis on which the interim and annual financial statements are presented and the SEC staff may ask the registrant to explain its basis for concluding that the impact is immaterial.

The SEC staff indicated that its views in this area are not meant to discourage registrants from complying with retrospective application in historical periods in situations in which the effect of adoption is immaterial to those prior periods. Rather, the SEC staff indicated that they expect registrants to evaluate the materiality of the retrospective adoption of the new accounting standard on historical financial statements.

Ms. Shah noted that in the past the SEC staff has provided certain filing accommodations when the adoption of a new accounting standard focused primarily on presentation within the financial statements and did not affect accounting measurements (e.g., the adoption of ASU 2011-5, *Comprehensive Income*, as discussed on the Highlights to the September 27, 2011 Joint Meeting). The SEC staff does not expect to provide similar specific accommodations in the future.

E. Supreme Court Decisions on the 2010 Patient Protection and Affordable Care Act

In response to the Committee's inquiry, Todd Hardiman noted that the SEC staff was aware that potential accounting and reporting ramifications may result if the Supreme Court ruled against the 2010 Patient Protection and Affordable Care Act, including possible accounting issues for registrants in various industries (e.g., healthcare providers, pharmaceutical companies, etc.) .

[Note: On June 28, the Supreme Court reached its decision and upheld the individual mandate "and other provisions" contained in the 2010 Patient Protection and Affordable Care Act.]

IV. IFRS WORK PLAN

Craig Olinger commented that the Office of the Chief Accountant is actively focusing on finalizing, summarizing and publishing its final report under the Work Plan. In May, SEC Commissioner Elisse Walter commented that the SEC staff expects to publish its final report under the Work Plan "in a matter of weeks." Mr. Olinger indicated that the final report is expected to comprehensively summarize the SEC's considerations to date with respect to the Work Plan. Mr. Olinger specifically noted that the SEC staff report will not include a recommendation for next steps.

[Note: On July 13, 2012, the Office of the Chief Accountant's staff issued its final report which can be found at http://www.sec.gov/spotlight/globalaccountingstandards/ifrs-work-plan-final-report.pdf]

V. CONFIDENTIAL REVIEWS OF INITIAL REGISTRATION STATEMENTS

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In April, the Jumpstart Our Business Startups Act (JOBS Act) was signed into law to encourage smaller companies to raise capital in the United States. The JOBS Act, which is discussed in more detail below, created a new category of public issuers called Emerging Growth Companies (EGC). Generally, an EGC is a company with annual revenues less than $1 billion and, following an initial public offering, less than $700 million in public float. Under the JOBS Act, an EGC may confidentially submit certain draft Securities Act registration statements to the SEC staff for confidential view.

Angela Crane indicated that to date the SEC staff has been able to review all confidential submissions within the Division's target 30-day review timeline when the registration statements initially submitted were substantially complete, as discussed in the response to Question 7 in the Frequently Asked Questions published by the SEC staff related to the JOBS Act Confidential Submission Process for EGCs. The SEC staff has seen instances where the company did not qualify as an EGC and other instances in which initial submissions of the registration statement were not substantially complete upon receipt. In those instances where the submission was not complete, the SEC staff will contact the registrant to inform it of this fact and will defer review until a substantially complete submission is made.

VI. IMPLEMENTATION AND INTERPRETATION OF RECENT SEC RELEASES

A. Sample Letter Sent to Financial Institutions Regarding Their Structured Note Offerings Disclosure in Their Prospectus Supplements and Exchange Act Reports (the "Sample Letter")

Ms. Shah indicated that the SEC staff published the Sample Letter, which was sent to certain financial institutions, to highlight areas in which institutions could improve disclosures about future structured note offerings. The Sample Letter was published as a result of reviews of prospectus supplements performed by SEC staff in the Office of Capital Markets and Trends with the objective of identifying ways to improve disclosures about the types of securities offered, structures of securities offered, risks to investors, etc. Ms. Shah indicated that given the Sample Letter was recently published in April 2012, it was too early for the SEC staff to share meaningful observations with respect to use of the guidance in practice.

Ms. Shah also noted that the Office of Capital Markets and Trends will continue to review prospectus supplements with the objective of identifying further trends. While the SEC staff may issue comments to a specific registrant if circumstances arise, the future prospectus supplement reviews are expected to be of broad focus.

B. CF Disclosure Guidance: Topic No. 5 – Staff Observations Regarding Disclosures of Smaller Financial Institutions

Mark Shannon indicated that the recently issued CF Disclosure Guidance: Topic No. 5 – Staff Observations Regarding Disclosures of Smaller Financial Institutions, which summarizes a number of observations by the SEC staff about MD&A and accounting policy disclosures of smaller financial institutions, is intended to update and expand upon information included in a slide deck covering the same subject previously posted on the SEC's web site. Mr. Shannon indicated that the guidance reflects the SEC staff's views on areas that are the subject of frequent comment to smaller financial institutions.

The SEC staff would welcome consideration of the guidance by financial institutions of varying sizes to the extent it was deemed applicable.

The Committee noted that the guidance has been well-received by registrants and has been recommended to financial institutions of all sizes.

VII. CAPITAL FORMATION INITIATIVES

A. Recommendations by the SEC Advisory Committee on Small and Emerging Businesses

Jennifer Zepralka commented that the JOBS Act addresses a lot of topics that had previously been the focus of the Advisory Committee on Small and Emerging Businesses. Ms. Zepralka indicated that now that the JOBS Act has been enacted, the Advisory Committee may focus on recommendations about rulemaking and other guidance under the Act (see below for a discussion of the JOBS Act-related efforts by the SEC staff). Additionally, Ms. Zepralka indicated that the Advisory Committee may consider whether to recommend extending some of the provisions of the JOBS Act to other types of companies that do not meet the definition of an EGC. For example, the Advisory Committee may consider whether other types of companies (e.g., non-EGC companies with public float between $75 million and $250 million) should be allowed to take advantage of the same or similar scaled disclosures (e.g., under Regulation S-K) as offered to EGCs or smaller reporting companies.

B. JOBS Act

Ms. Zepralka indicated that since the enactment of the JOBS Act in April 2012, the SEC staff has undertaken a number of actions to issue pragmatic guidance designed to ensure the provisions of the Act are applied in practice in a manner consistent with the intent of Congress. The SEC has posted on its web site several *Frequently Asked Questions* documents designed to provide guidance about how to implement the provisions of Title I of the JOBS Act regarding emerging growth companies as well as Titles V and VI.

Ms. Shah indicated that the SEC staff is still evaluating some of the more complex implementation issues for Title I (e.g., how the provisions apply to reverse mergers, shell companies, acquisitions, etc.) and may publish additional guidance in the future related to these issues.

[Note: The SEC's Division of Corporation Finance has established a web page devoted to JOBS Act information which can be found at http://www.sec.gov/divisions/corpfin/cfjobsact.shtml]

Ms. Zepralka also discussed two studies that the SEC staff has undertaken as required by the provisions of the JOBS Act. The first study, which is required to be submitted within 90 days of the enactment of the JOBS Act, focuses on trading and quoting securities in penny increments (commonly known as "decimalization"). The second study, which has a 180-day deadline, is a comprehensive review of Regulation S-K to determine how it can be updated to modernize and simplify the registration process and reduce the costs and other burdens for EGCs.

[Note: The Commission issued the report of the decimalization study on July 20, 2012, which can be found at http://www.sec.gov/news/studies/2012/decimalization-072012.pdf]

Regarding the SEC's rulemaking related to the JOBS Act, Ms. Zepralka noted that the SEC staff has begun efforts for rulemaking under Titles II, III and IV, as well as rule changes to implement Titles V and VI. Finally, Ms. Zepralka also indicated that the SEC staff has begun the outreach efforts required under Title VII to educate minority-, women- and veteran-owned businesses, as well as small and medium sized businesses, about the JOBS Act.

VIII. SEC STAFF AND OTHER INITIATIVES

A. Financial Reporting Manual

Michael Stehlik noted that the next update to the Division's Financial Reporting Manual (FRM) is expected to be issued soon, with updates dated as of March 31, 2012. Mr. Stehlik indicated that the incorporation of issues and highlights of the International Practices Task Force into the FRM is an ongoing effort and will be reflected in a future version of the FRM.

[Note: On July 11, 2012, the Division's staff issued its quarterly update of the FRM.]

B. Status of Rulemaking for Conflict Minerals and Extractive Industry Payments

The SEC staff continues to work on the rulemaking for conflict minerals and extractive industry payments.

[Note: The Commission subsequently scheduled an open meeting on August22, 2012 to consider adopting final rules on conflict minerals and payments by resource extraction issuers.]

IX. CURRENT PRACTICE ISSUES

A. Measuring Significance of "Related Businesses" Under the Income Test

The SEC staff discussed recent additions to the FRM provided to assist registrants in assessing significance of acquisitions of related businesses. Under Rule 3-05(a)(3) of Regulation S-X, businesses shall be deemed related if:

(i) They are under common control or management;
(ii) The acquisition of one business is conditional on the acquisition of each other business; or
(iii) Each acquisition is conditioned on a single common event.

The SEC staff revised Section 2020.8 to the FRM as follows:

> Related businesses must be treated as a single business when measuring significance. For purposes of the income test, use absolute values when some of those related businesses report losses and others report income. If the significance level is met, financial statements of each of the related businesses are required, except that businesses that are under common control or management may be presented on a combined basis. If the registrant believes that this application of the significance test results in a requirement to present financial statements of one or more related businesses that are not reasonably necessary to inform investors, the registrant may make a request to CF-OCA for relief. [emphasis added]

Mr. Hardiman indicated that FRM Section 2020.8 was revised to provide guidance in response to "put-together" transactions in which previously unrelated business are acquired at one time (often in connection with an IPO) and other transactions in which the acquired businesses are deemed related under criteria (ii) and (iii) of Rule 3-05(a)(3) of Regulation S-X (i.e., the acquired businesses were not under common control or management).

The SEC staff indicated that the guidance added to FRM Section 2020.8 was not intended to be applied to acquisitions of multiple businesses that qualify for presentation of combined financial statements (i.e., the acquired businesses have been under common control or management for the period covered by the income test). The SEC staff indicated that it is considering whether to clarify the guidance in the FRM.

B. Financial Reporting Requirements in a Reverse Spinoff

The SEC staff discussed the pre- and post-spinoff financial reporting requirements for the legal spinnee and the legal spinnor in connection with a divestiture transaction known as a reverse spinoff. The SEC staff did not express any views as to the appropriate reporting. The SEC staff will continue to evaluate the various reporting requirements for the legal spinnee and legal spinnor in reverse spinoffs and will consider whether or not further guidance should be provided in this area.

To illustrate the potential issues with respect to the financial reporting requirements for reverse spinoffs, the following example was considered:

> *Example:* ParentCo is an SEC registrant. ParentCo is a holding company with two 100% owned subsidiaries: BigSub and LittleSub. ParentCo has no assets, liabilities or operations other than its investments in BigSub and LittleSub. None of the entities involved qualify as an "emerging growth company."

Each year, ParentCo's consolidated income statement is comprised of the following results (for simplicity, ParentCo, BigSub and LittleSub are assumed to have the same results for all periods):

	ParentCo Consolidated	**BigSub**	**LittleSub**
Revenues	**$ 100**	**$ 80**	**$ 20**
Expenses	**(80)**	**(40)**	**(40)**
Net income	**$20**	**$40**	**($20)**

ParentCo intends to separate the operations of BigSub and LittleSub through a transaction which will take the legal form of distributing the common stock of BigSub to ParentCo's shareholders in a pro-rata distribution (i.e., from a legal perspective, ParentCo will spinoff the operations of BigSub and will retain the operations of LittleSub).

ParentCo will prepare a Form 10 to register the shares of BigSub under the Exchange Act (there will not be a shareholder vote/proxy statement).

ParentCo has properly determined that the transaction should be accounted for as a reverse spinoff.

In the fact pattern above, BigSub is the accounting “spinnor” and the legal “spinnee.” ParentCo and LittleSub, together on a combined basis, are the accounting spinnee and legal spinnor.

The existing SEC guidance in this area resides in Section 2120.3 of the FRM, which states "[i]f disposition of a business is being accomplished through the registrant’s distribution to shareholders of its ownership interests in that business, audited financial statements of the separate legal "spinnee" (which may not be the spinnee for accounting purposes) for the same periods required for the registrant are required in a Form 10 or 1933 Act registration statement filed in connection with the spinoff."

FASB guidance relating to spinoffs (ASC 505-60-25-4) states "[i]n a reverse spinoff, the legal spinnee shall be treated as though it were the spinnor for accounting purposes (accounting spinnor)." In other words, in a reverse spinoff, the legal spinnee should be treated as the continuing entity (i.e., as if it had disposed of the operations of the legal spinnor).

As noted above, the SEC staff will continue to evaluate the various reporting requirements for the legal spinnee and legal spinnor in reverse spinoffs and will consider whether or not further guidance should be provided in this area.