

SEC in Focus



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SEC staff turns to JOBS Act implementation

The SEC staff has been busy addressing implementation questions about the recently enacted Jumpstart Our Business Startups Act (JOBS Act), especially for emerging growth companies (EGCs).

Provisions in Title I of the JOBS Act related to EGCs are effective immediately and do not require SEC rulemaking. But many questions have arisen.

The staff of the SEC’s Division of Corporation Finance has issued a series of Frequently Asked Questions¹ on (1) EGC eligibility and disclosure, (2) confidential submission of EGC registration statements and (3) the amended registration and deregistration record holder thresholds in Section 12(g) of the Exchange Act. The SEC staff also has implemented a secure email system² to accept confidential submissions and has released specific instructions on how to use it.

Title I of the JOBS Act created the new emerging growth company category of issuer to encourage initial public offerings. Certain regulatory requirements are phased in for EGCs during a five-year initial public offering (IPO) “on-ramp” period. The JOBS Act also modified triggers for public registration and reporting by amending Section 12(g) of the Exchange Act to increase the number of record holders that trigger a company’s obligation to register and report as a public company.

The JOBS Act encourages capital formation through other provisions that require SEC rulemaking. These provisions include (1) a new category of exempt offerings of up to \$50 million raised over a 12-month period, (2) revisions to exempt securities offerings under Rule 506 of Regulation D to allow general solicitation in offers and sales of securities if the purchaser of the security is an accredited investor (90 days from enactment) and (3) allowing private companies to raise small amounts of capital from a large group of investors through a process called crowdfunding without adding to the record holder count that triggers Exchange Act registration (270 days from enactment). The SEC will hold an open meeting on 22 August 2012 to consider rules to allow general solicitation and advertising in securities offerings under Rules 506 of Regulation D and 144A of the Securities Act.



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- ▶ *Technical Line, Implementing the JOBS Act (SCORE No. CC0348)*
- ▶ *To the Point, JOBS Act to promote capital formation (SCORE No. CC0345)*

The SEC also will need to engage in certain studies required by the JOBS Act, such as simplifying the Regulation S-K nonfinancial disclosures for EGCs. The SEC is seeking public comment³ before proposing new rules or amendments required by the JOBS Act.

SEC staff revises its nonpublic submission policy for foreign private issuers

The Division of Corporation Finance staff revised its policy⁴ for the nonpublic submission of initial registration statements by foreign private issuers (FPIs) to be consistent with its confidential submission policy for EGCs. The SEC staff previously has allowed certain FPIs and foreign governments to submit initial registration statements on a confidential basis. Under the old policy, draft registration statements, staff comments and issuer responses that were made prior to the FPI's first public filing remained confidential.

The revised policy requires eligible FPIs to publicly file all nonpublic draft registration statements as exhibits to their first public registration statement. In addition, all SEC staff comments and FPI responses will be posted on EDGAR following completion of the registration process. The new policy is effective for FPIs submitting initial drafts after 30 May 2012.

SEC rulemaking

Final rules

Listing standards for compensation committees

The SEC issued a final rule directing national securities exchanges to adopt minimum listing standards related to compensation committees and their use of compensation consultants, independent legal counsel and other advisers.⁵ The SEC also amended proxy rules to require new disclosures about whether the use of compensation consultants raised any conflicts of interest.

The final rule and rule amendments are required by Section 952 of the Dodd-Frank Act, which created Section 10C of the Securities Exchange Act of 1934. This section requires the SEC to direct exchanges to prohibit the listing of companies that don't comply with the new compensation committee requirements.

Exchanges must propose their listing standards no later than 90 days after the rule's effective date, which is 30 days after publication in the Federal Register. The SEC has one year from the effective date to approve the listing standards. The new proxy disclosure requirements go into effect for shareholder meetings on or after 1 January 2013 at which directors are elected.

Several Dodd-Frank Act rules continue to be delayed

Some rules required by the Dodd-Frank Act continue to be delayed. The following final and proposed rules were included in the SEC's timeline for completion by June 2012, but will shift to the second half of 2012:⁶

- ▶ *Adopt final rule regarding risk retention by securitizers of asset-backed securities (Section 941)*
- ▶ *Propose enhanced compensation disclosure rules for pay for performance, pay ratios and hedging by employers and directors (Sections 953 and 955)*

SEC rulemaking update for the second quarter of 2012

- ▶ *Listing standards for compensation committees*
- ▶ *Several Dodd-Frank Act rules continue to be delayed*
- ▶ *IFRS Work Plan update*

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- ▶ *To the Point, SEC requires listing standards for compensation committees (SCORE No. CC0351)*
- ▶ *To the Point, Support grows for keeping US GAAP but basing future standards on IFRS (SCORE No. BB2229)*

- ▶ *Propose “clawback” of executive incentive-based compensation rules (Section 954)*
- ▶ *Adopt final conflict mineral disclosure rules (Section 1502)*
- ▶ *Adopt final resource extraction disclosure rules (Section 1504)*

The SEC announced that it will hold an open meeting on 22 August 2012 to consider adoption of final rules related to Sections 1502 and 1504 on conflict minerals and resource extraction disclosures.

IFRS Work Plan update

In June 2012, SEC Deputy Chief Accountant Julie Erhardt said that the final Work Plan would likely be released in the coming “weeks and not months.” The SEC staff stated in December 2011 that, while it had completed the majority of fieldwork related to its Work Plan, it needed a few additional months to produce a final report.

The staff of the Office of the Chief Accountant is executing a comprehensive Work Plan that addresses specific areas of concern to help the SEC Commissioners decide whether and, if so, how to incorporate International Financial Reporting Standards (IFRS) into the US financial reporting system.

Other SEC activities

SEC Advisory Committee on Small and Emerging Companies meets

The SEC Advisory Committee on Small and Emerging Companies (the Committee) did not make any recommendations at its 8 June 2012 meeting, but it discussed implementation of the JOBS Act and related rulemaking, as well as other rules and regulations affecting small and emerging companies.

For example, the Committee discussed the required revisions to Rule 506 of Regulation D and the requirement for an issuer to take “reasonable steps” to verify that all purchasers are accredited investors. The Committee provided its input to the SEC staff on the pending revisions to Regulation D, including what constitutes “reasonable steps.”

The Committee plans to meet in September 2012 and is expected to continue its focus on scaling disclosure and corporate governance rules for smaller public companies. It also may serve as a resource to the SEC as it conducts rulemaking required by the JOBS Act.

The Committee focuses on the priorities and interests of small privately held businesses and publicly traded companies with capitalizations of \$250 million or less.

Investor Advisory Committee holds inaugural meeting

The SEC’s Investor Advisory Committee held its first meeting on 12 June 2012 to introduce its members, elect officers and consider by-laws and a charter. It also discussed the implementation of the Dodd-Frank Act, investor protection under the JOBS Act and other issues.

The Investor Advisory Committee was formed in April 2012 under the requirements of the Dodd-Frank Act to advise the Commission on, among other things, regulatory priorities, the effectiveness of disclosure and various investor protection initiatives.

Other SEC and SEC staff actions and guidance in the second quarter of 2012

- ▶ *SEC Advisory Committee on Small and Emerging Companies meets*
- ▶ *Investor Advisory Committee holds inaugural meeting*
- ▶ *2009 US GAAP XBRL Taxonomy phased out*
- ▶ *Staff observations about disclosures of smaller financial institutions*

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- ▶ [Technical Line, Using the 2012 XBRL US GAAP Taxonomy \(SCORE No. BB2313\)](#)

2009 US GAAP XBRL Taxonomy phased out

Effective 2 July 2012, EDGAR will no longer accept XBRL exhibits using the 2009 US GAAP XBRL Taxonomy. Registrants may continue to use the 2011 US GAAP XBRL Taxonomy, but the SEC staff strongly encourages companies to adopt the latest version for their XBRL exhibits (i.e., the 2012 taxonomy released in March 2012). Details about the taxonomies can be found on the FASB and SEC websites.⁷

SEC staff observations about disclosures of smaller financial institutions

To help registrants enhance their disclosures, the SEC Division of Corporation Finance (Division) compiled a summary of comments it frequently raises in its reviews of filings of smaller financial institutions. When preparing their filings with the SEC, registrants should consider the Division staff's observations that are included in CF Disclosure Guidance: Topic 5,⁸ *Staff Observations Regarding Disclosures of Smaller Financial Institutions*.

Securities markets

Nasdaq proposes changes to director independence listing rules

Nasdaq has proposed a rule to broaden an exception in its corporate governance listing rules that would permit one non-independent director to serve on the audit, nominating or compensation committees of a listed company under exceptional circumstances, and with proper disclosure for up to two years.

Current listing standards preclude a director who has a family member who is an employee of a listed company from using this exception. The rule proposal would allow a director who is a family member of a nonexecutive employee of a listed company to use this exception to serve on the listed company's audit committee, compensation committee or nominating committee. Prohibitions would still apply to directors who are family members of an executive employee.

Under both the current and proposed exception, a listed company's board of directors must make an affirmative determination that the non-independent director's membership on a committee is in the best interests of the company and its stockholders.

The comment period for the proposal ended in June 2012.

SEC approves proposals to address extraordinary volatility

The SEC approved two proposals submitted by the national securities exchanges and the Financial Industry Regulatory Authority (FINRA) to address extraordinary volatility in individual securities and the broader US stock market. Each of the proposals has been approved for a one-year pilot program. These changes will be implemented by the exchanges and FINRA by February 2013.

The first initiative, "limit up-limit down," is a mechanism that prevents trades in individual exchange-listed stocks from occurring outside of a specified price band. This new mechanism will replace the existing single-stock circuit breakers that the Commission approved on a pilot basis after the market events of 6 May 2010. The second initiative updates existing market-wide circuit breakers that, when triggered, halt trading in all exchange-listed securities throughout the US markets.

Current practice issues

Timing of retrospective revision of financial statements upon adoption of a new accounting standard

The SEC staff recently said it does not expect to continue to explicitly provide accommodations allowing abbreviated disclosures in registration statements in lieu of filing annual financial statements retrospectively revised for the subsequent adoption of accounting standards updates. Instead, the SEC staff said companies and their auditors need to determine whether to retrospectively revise their annual financial statements based on the materiality of the change resulting from adopting the new standard.

New accounting standards increasingly require retrospective application. When that is the case, companies usually must revise historical annual financial statements that are included or incorporated by reference in new or amended registration statements, after they file interim financial statements that reflect the adoption of the standard. For the retrospective application of ASU 2011-05 and ASU 2011-12 related to the presentation of comprehensive income, the SEC staff said it would not object if a registrant concludes, and its auditor agrees, that it does not need to retrospectively revise previously issued annual financial statements incorporated by reference into a new or amended registration statement as long as the registration statement, or an incorporated Form 8-K, includes prominent and transparent disclosure of the information required by the standards. However, the SEC staff has indicated that such accommodation would not be extended to future accounting standards updates.

Personnel changes

Personnel changes

- ▶ *Chief Accountant leaving the SEC*
- ▶ *Director of Division of Investment Management to retire*

Chief Accountant leaving the SEC

James Kroeker, the SEC's Chief Accountant, will leave the SEC in July 2012. Mr. Kroeker joined the SEC in 2007 as Deputy Chief Accountant and has been Chief Accountant since January 2009. In that role, he has counseled the Commission on a wide range of accounting and auditing issues, including its IFRS Work Plan. SEC Chairman Mary Schapiro said Mr. Kroeker "provided superb counsel on a range of accounting and auditing related matters and has always stressed the importance of accounting to our investor protection mission."



James Kroeker

Director of Division of Investment Management to retire

Eileen Rominger, Director of the Division of Investment Management, will retire this July after serving in that role since early 2011. Chairman Schapiro said Ms. Rominger "understood the importance of a fair and efficient investment management industry to the well-being of investors everywhere. Her practical insights and steady leadership served investors well."

Selected enforcement actions

SEC sues two executives to recover bonuses and stock profits

Two former executives of a surgical products manufacturer were sued by the SEC to recover bonus compensation and stock sale profits they received after the company filed materially misstated financial statements.

The executives are not charged with personal misconduct, but they are required under Section 304 of the Sarbanes-Oxley Act to reimburse the company for bonuses and stock profits that they received as a result of the accounting restatement. This section provides for reimbursement by CEOs and CFOs of certain compensation and stock sale profits received while their companies were in material noncompliance with financial reporting requirements due to misconduct. The “clawback” provision applies even if those executives are not personally charged with the underlying misconduct or alleged to have otherwise violated the federal securities laws.

Company settles subprime mortgage investment charges

The SEC charged a mortgage company with misleading investors in several offerings of subprime residential mortgage-backed securities (RMBS) by failing to disclose that its financial condition was significantly deteriorating.

The mortgage company allegedly promised investors in more than \$4 billion of RMBS offerings that it sponsored in early 2007 that it would repurchase or replace mortgages that breached representations and warranties. However, the company failed to tell investors about its deteriorating financial condition and that it could not meet its repurchase obligations with existing resources.

The company agreed to pay \$28.2 million to settle the SEC’s charges.

“Clawback of incentive compensation and stock sale profits as authorized under the Sarbanes-Oxley Act is yet another reason for CEOs and CFOs to be vigilant.”

– Robert Khuzami, Director of the SEC’s Division of Enforcement

What’s next at the SEC?

- ▶ The JOBS Act requires the SEC to take a number of actions, including identifying ways to simplify Regulation S-K for EGCs, studying whether to designate a minimum increment for trading and quoting EGC securities and revising rules, including those to eliminate the prohibition against general solicitation or advertising in Regulation D exempt offerings to accredited investors. The SEC will consider proposed rules on modifications to Regulation D at its 22 August 2012 open meeting.
- ▶ We expect the SEC staff to continue issuing interpretive guidance about implementation of the JOBS Act.
- ▶ The Office of the Chief Accountant is expected to publish a final report on the IFRS Work Plan soon.
- ▶ The SEC continues to focus on implementing the Dodd-Frank Act. An open meeting is planned for 22 August 2012 to consider adoption of final rules related to conflict minerals and resource extraction disclosures.

Endnotes:

- ¹ SEC staff guidance, including its FAQs about the JOBS Act, is available on the SEC's website at <http://www.sec.gov/divisions/corpfin/cfjobsact.shtml>.
- ² On 28 June 2012, the SEC staff announced that it is working to implement an EDGAR-based system that will replace the secure email system. Companies should continue to use the email system until further notice from the SEC.
- ³ Comments on the JOBS Act may be submitted to the SEC at <http://www.sec.gov/spotlight/jobsactcomments.shtml>.
- ⁴ The revised policy is available at <http://sec.gov/divisions/corpfin/internatl/nonpublicsubmissions.htm>.
- ⁵ The final rule is on the SEC website at <http://www.sec.gov/rules/final/2012/33-9330.pdf>. A related press release and fact sheet are also on the website at <http://www.sec.gov/news/press/2012/2012-115.htm>.
- ⁶ The SEC Dodd-Frank Act timeline is available at <http://www.sec.gov/spotlight/dodd-frank.shtml>.
- ⁷ Details about the taxonomies can be found on the FASB and SEC websites available at <http://www.fasb.org> and <http://xbrl.sec.gov>, respectively.
- ⁸ CF Disclosure Guidance: Topic 5 is available at <http://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic5.htm>.

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