

SEC Staff Updates Financial Reporting Manual

On November 9, 2016, the SEC's Division of Corporation Finance (the "Division") revised certain sections of its [Financial Reporting Manual](#) (FRM).¹ The most notable changes (1) clarify when pro forma financial information required by Regulation S-X, Article 11,² can be omitted from an initial public offering (IPO) for an emerging growth company (EGC); (2) clarify when an EGC may present two years of target financial statements in a proxy statement;³ and (3) add guidance on the implementation of the FASB's standards on leases ([ASU 2016-02](#)⁴), disclosures about short-duration contracts ([ASU 2015-09](#)⁵), and the preparation pro forma information subsequent to adoption of the new revenue recognition standard ([ASU 2014-09](#)⁶), as amended by [ASU 2015-14](#).⁷

These revisions are discussed below in more detail.

The Division updated paragraph 10220.5 of Topic 10, "Emerging Growth Companies," to clarify that, in a manner consistent with requirements of the Fixing America's Surface Transportation Act for financial statements, an EGC may omit pro forma financial information required by Article 11 from the registration statement for its IPO on Form S-1 or Form F-1 if the issuer reasonably believes that the information will not be required at the time of the offering.

The Division also added paragraph 10220.7, which states:

To the extent that target financial statements are required in a proxy statement . . . , the staff will not object if two years of the target's annual financial statements and interim financial statements are presented in a proxy statement filed after the legal acquirer's initial public offering of common equity securities but prior to the filing or the filing deadline of the legal acquirer's *first* Form 10-K only if:

- The legal acquirer is an EGC that is not a shell company, or
- The legal acquirer is a shell company EGC (such as a [special-purpose acquisition corporation] EGC) and the target would be an EGC if it were conducting an initial public offering of common equity securities.

The Division updated Topic 11, "Reporting Issues Related to Adoption of New Accounting Standards," to add:

A summary of the implementation guidance for the leases standard and a Q&A on the date of initial application of the leases standard in the context of a new registration statement. The leases standard requires companies to transition to the new standard in the year of adoption using a modified retrospective approach. This adoption approach requires that companies recognize and measure all leases within the scope of the standard that exist as of

¹ Division of Corporation Finance *Financial Reporting Manual*. The manual includes staff interpretations that, although helpful, are not authoritative. Before reaching any conclusion about appropriate financial reporting, registrants should carefully analyze their specific facts and circumstances, authoritative accounting literature, and SEC requirements.

² SEC Regulation S-X, Article 11, "Pro Forma Financial Information."

³ See Section 1140.3 of the FRM for a summary of the requirements for acquirer and target financial statements in proxy statements.

⁴ FASB Accounting Standards Update No. 2016-02, *Leases*.

⁵ FASB Accounting Standards Update No. 2015-09, *Disclosures About Short-Duration Contracts*.

⁶ FASB Accounting Standards Update No. 2014-09, *Revenue From Contracts With Customers*.

⁷ FASB Accounting Standards Update No. 2015-14, *Revenue From Contracts With Customers (Topic 606): Deferral of the Effective Date*.

the beginning of the earliest comparative period presented,⁸ referred to as the date of initial application. For example, the date of initial application is typically January 1, 2017, for a calendar-year company that adopts the new leases standard on January 1, 2019, because that will be the first day of the comparative three-year period presented in the December 31, 2019, financial statements in the year of adoption. The Q&A clarifies that, in this adoption fact pattern, if a company files a new registration statement after the first quarter of adoption but before the filing of the December 31, 2019, Form 10-K, the date of initial application would still be January 1, 2017. This fact pattern assumes that the new registration statement would require the financial statements for the fiscal years ended December 31, 2018, 2017, and 2016, along with any required fiscal 2019 interim financial statements. The Q&A also clarifies that reissuance of the financial statements in the new registration statement would accelerate the requirement to retroactively restate financial statements for the years ended December 31, 2018, and 2017, but it does not change the date of initial application. As such, the financial statements for the year ended December 31, 2016, that are included or incorporated by reference in the new registration statement would not be retrospectively restated.

- **Implementation guidance for disclosures about short-duration contracts**, including a Q&A indicating that after adopting ASU 2015-09 registrants do not have to separately provide the 10-year loss reserve table identified in Industry Guide 6⁹ in either the Business or MD&A section (in addition to the claims development tables now required by this new standard that are disclosed in the footnotes to the financial statements), but may choose to do so.
- **A Q&A on pro forma financial information provided in the year of adoption of the new revenue standard**, which clarifies that pro forma financial information prepared under Article 11 required to be filed after the first quarter adoption of the new revenue standard (using the full retrospective method) but before the issuance of the year-end Form 10-K that retrospectively recasts the annual financial statements presented, is not required to be updated to reflect the full retrospective adoption of the new revenue standard for periods preceding adoption. However, registrants are encouraged to provide appropriate disclosures if the effect of the new revenue standard on the respective historical period is material.

Example

If a registrant adopts the new revenue standard on January 1, 2018, using the full retrospective method, completes a significant acquisition in August 2018, and later files a Form 8-K that includes pro forma financial information for the year ended December 31, 2017, and the six months ending June 30, 2018, the registrant would not be required to reflect the adoption of the new revenue standard in the pro forma financial information for the year ended December 31, 2017. However, disclosure may be considered to address the comparability of the information presented.

Editor's Note: The SEC staff has reminded registrants about best practices to follow in the periods leading up to the adoption of the new revenue and leases standards. The staff's comments, which reiterate themes it has addressed over the past year, have focused on internal controls over financial reporting, auditor independence, and disclosures related to implementation activities. See Deloitte's September 22, 2016, [Financial Reporting Alert 16-3, SEC Reminds Registrants of Best Practices for Implementing New Revenue, Lease, and Credit Loss Accounting Standards](#), for a discussion of these best practices and SEC staff reminders. Registrants should proactively assess the impact of these new standards, monitor implementation issues, and be mindful of the importance of transparent disclosure that discusses the effects of adoption.

⁸ Adoption is subject to certain practical expedients and other transition relief prescribed by the standard.

⁹ Securities and Exchange Commission Securities Act Industry Guide No. 6, *Disclosures Concerning Unpaid Claims and Claim Adjustment Expenses of Property-Casualty Insurance Underwriters*.

Other changes listed in the SEC's [summary](#) of changes to the FRM include amendments to (1) paragraph 1330.5 that clarify 10-K filing requirements after effectiveness of Form 10, in certain fact patterns, and (2) paragraph 5120.1 that "clarify the effect of loss of smaller reporting company status on accelerated filer determination and filing due dates."

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