

Is going public the right answer for your company?

Key regulations and reporting requirements

During the course of an IPO, underwriters, lawyers and accountants invariably will refer to various U.S. securities laws, regulations and accounting standards applicable to public companies. You may be familiar with a few of these requirements. Others — not so much.

Here, we outline some of the more significant laws and regulations applicable to public companies and companies going through the IPO process. Compliance with these requirements can be operationally challenging and time-consuming. But failure to observe the rules can bring severe penalties for the company and its officers, and could even stall or quash the IPO. It is therefore critical to involve qualified legal, financial and accounting advisers to help your company navigate through the complexities of the securities laws and regulations.

Securities Act of 1933¹ (Securities Act) and Securities Exchange Act of 1934² (Exchange Act): The Securities Act requires the offering of securities to be registered with the SEC before they are sold to the public. The individual Securities Act registration statement form used (such as [Form S-1](#), used in the vast majority of IPOs) defines the content required in the registration statement. The forms include specific references to certain regulations that lay out the reporting requirements. [Regulation S-K](#) governs disclosure of information outside the financial statements, while [Regulation S-X](#) governs the form and content of the financial statements.

After registration becomes effective, an entity would then be subject to periodic and current reporting requirements under the Exchange Act, including:

Type of filing	Filing timeline
Annual report on Form 10-K	Within 60–90 days after fiscal year-end, depending on the company's filing status
Quarterly report on Form 10-Q	Within 40–45 days after each fiscal quarter-end, depending on the company's filing status
Other material information on Form 8-K	Generally within four business days after the material event occurs

¹ [See link](#) for more information about the Securities Act.

² [See link](#) for more information about the Exchange Act.





Jumpstart Our Business Startups (JOBS) Act³

The JOBS Act, signed into law in 2012, was designed to make it easier for so-called emerging growth companies (EGCs) to raise capital. An EGC is a company with revenues in its latest fiscal year of less than \$1.07 billion⁴ that has not met any other disqualifying provisions. EGCs are permitted to make confidential submissions of draft registration statements to the SEC during the IPO process, which must become public at least 15 days before the company goes on its roadshow⁵. EGCs are also permitted to scale back certain disclosures for a period of up to five years — including those regarding executive compensation — in both the IPO registration statement and in subsequent periodic filings.

Dodd-Frank Wall Street Reform and Consumer Protection (Dodd-Frank) Act of 2010⁶

Issued in the aftermath of the global financial crisis in 2008, the Dodd-Frank Act was primarily designed to enhance corporate governance practices. For example, the Dodd-Frank Act requires public companies to:

- Disclose why they have combined or separated the roles of chairman and CEO
- Periodically hold a nonbinding shareholder vote on executive compensation, known as a “say on pay”; note that EGCs are exempt from this requirement

Sarbanes-Oxley Act of 2002⁷

The Sarbanes-Oxley Act was signed into law in 2002 following the Enron scandal. This sweeping legislation contains a number of provisions affecting public companies, including the following:

Section 404 mandates that management — and in some cases, the company’s external auditors — provide an opinion on the company’s internal control over financial reporting (ICFR). In simplest terms, ICFR represents the processes, checks and balances a company has in place to ensure the financial statements are fairly presented and free of material errors.

A focus on Section 404

Compliance with Section 404 requires enormous effort. A company will typically spend more than half a year identifying its key controls and testing that they are operating effectively. Unfortunately, this extensive level of testing is unavoidable. Simply put, it’s the only way a company can be in a position to evaluate and disclose the effectiveness of its ICFR.

Proper implementation will typically require hiring additional staff and, for some, the purchase of new financial reporting systems. Many public companies will also be required to have their ICFR audited by an independent accounting firm. The only exceptions are for:

- EGCs (for a period of up to five years)
- Non-accelerated filers (companies with public float of less than \$75 million)

A newly public company is not required to provide a management assessment or, if applicable, an auditor’s report, on ICFR until it files its second annual report with the SEC.

³ [See link](#) for an overview of the JOBS Act, along with a link to the full text.

⁴ The SEC is required to adjust the total gross revenue amount to inflation every five years. The total gross revenue amount was last updated on April 12, 2017.

⁵ In 2017, the SEC staff began accepting certain voluntary draft registration statement submissions for non-public review from all issuers.

⁶ [See link](#) for more information about the Dodd-Frank Act.

⁷ [See link](#) for an overview of the Sarbanes-Oxley Act, along with a link to the full text.

Section 302 requires certifications in quarterly and annual periodic reports from both the CEO and CFO that:

- They have read the entire Form 10-K or Form 10-Q.
- The report contains no material misstatements or omissions.
- The financial statements and related information are fairly presented in all material respects.
- They are responsible for the design of disclosure controls and procedures — that is, the systems and communication processes to ensure that the required information is reported in Forms 10-K and 10-Q in a timely fashion — and ICFR, and have concluded whether they are operating effectively.
- The company has disclosed any material changes in the company's ICFR during the quarter.
- They have communicated to the audit committee and the external auditors all significant deficiencies and material weaknesses in ICFR, as well as any fraud perpetrated by persons significantly involved with ICFR (whether material or not).

Section 906 requires an additional certification by the CEO and CFO that the Forms 10-Q and 10-K comply with the Exchange Act, and that the filing fairly presents the financial condition and operating results of the company. Section 906 also prescribes the penalties for making false certifications — up to 20 years in prison and/or up to a \$5 million fine.

Section 201 enhances rules regarding auditor independence.⁸ To avoid conflicts of interest, external audit firms are prohibited from providing nonaudit services to public clients contemporaneously with the audit. These prohibited services include — but are not limited to — bookkeeping, performing management functions, financial information systems design and implementation, and appraisal or valuation services, as well as acting as an expert witness or advocating on a client's behalf. Violation of independence rules has serious consequences. For this reason, a company contemplating going public should assess nonaudit services performed by its independent auditor for compliance with the independence rules. In addition, these companies should have ongoing processes in place to periodically monitor continued compliance with auditor independence regulations.

Other requirements the Sarbanes-Oxley Act imposes on public companies include the following:

- Mandates that the majority of the board of directors be composed of independent persons
- Requires that the audit committee be made up entirely of independent directors, and disclosure of whether at least one audit committee member is a financial expert
- Compels the audit committee to preapprove all audit and nonaudit services provided by the external auditor
- Prohibits many types of personal loans between the company and its directors and executive officers
- Requires disclosure of whether the company has adopted codes of ethics for senior officers

⁸ Since the passage of the Sarbanes-Oxley Act, auditor independence rules have been further fine-tuned by the SEC and the Public Company Accounting Oversight Board.



Foreign Corrupt Practices Act of 1977⁹ (FCPA)

The FCPA requires companies to maintain accurate books and records, and prohibits bribery of public officials. The penalties for failing to comply with the FCPA are severe and can include fines in the hundreds of millions of dollars.

Regulation G (Reg G)¹⁰

Many public companies report non-GAAP financial measures — such as EBITDA — in their public disclosures. Reg G precludes companies from presenting non-GAAP metrics that are misleading, and requires disclosure of:

- The most directly comparable figure presented in accordance with GAAP
- A reconciliation of that GAAP figure to the non-GAAP measure

Regulation Fair Disclosure¹¹

This regulation precludes companies from providing material nonpublic information to certain select individuals, such as favored analysts. Instead, material nonpublic information should be disclosed to all potentially interested parties simultaneously or within a short time period. After an IPO, such disclosure ordinarily is provided on a Form 8-K and the company's website.

Exchange listing requirements

Each stock exchange has its own set of initial listing requirements that a company must meet to begin trading on that exchange, as well as continued standards to maintain its listing. Requirements include financial and nonfinancial standards, in areas such as market value of publicly held shares, stock price, annual revenues or pretax net income metrics and governance requirements. For instance, as it relates to governance, companies listed on the Nasdaq exchange must have an independent compensation committee with at least two members. This committee must determine, or recommend to the full board for determination, the compensation of the CEO and all other executive officers. The New York Stock Exchange contains similar listing requirements.

Financial accounting and disclosure requirements¹²

U.S. GAAP contains a number of accommodations for private companies. For example, private companies that are not in the process of going public are often allowed to present abbreviated disclosures. More recently, with the creation of the Public Company Council (PCC), additional simplified accounting alternatives are available to companies not meeting the definition of a public business entity. An IPO company may not avail itself of these simplified accounting alternatives.

During the registration process and thereafter, a company must prepare its financial statements using public company GAAP. In addition, public companies also must abide by SEC regulations and interpretations of U.S. GAAP, and provide additional disclosures in certain instances.

⁹ [See link](#) for an overview of the FCPA, along with a link to the full text.

¹⁰ SEC Release Nos. 33-8176; 34-47226; FR-65; File No. S7-43-02, Conditions for Use of Non-GAAP Financial Measures, March 28, 2003. [See link](#) for the full text of this rule.

Reg G applies to any public disclosure, including press releases and investor presentations. Regulation S-K Item 10(e) applies to registration statements, periodic reports and other documents filed with the SEC that include non-GAAP financial measures. For instance, S-K Item 10(e) would apply to non-GAAP financial measures included within Management's Discussion and Analysis in Form S-1 and Form 10-K.

¹¹ SEC Release Nos. 33-7881, 34-43154, IC-24599, File No. S7-31-99, Selective Disclosure and Insider Trading, October 23, 2000. [See link](#) for the full text of this rule.

¹² This section pertains to companies preparing financial statements in accordance with U.S. GAAP. Foreign private issuers may provide financial statements prepared in accordance with International Financial Reporting Standards as issued by the IASB.

The following discussion highlights some of the main areas in which financial reporting for private and public companies differ. It is certainly not intended to be an exhaustive examination of all potential differences.



Earnings per share (EPS)

Public companies are required to present EPS in both their IPO registration statement and any subsequent Forms 10-K and 10-Q. Calculating EPS can be complex — especially for companies that issue several different classes of equity.



Segment reporting

Public companies must disclose disaggregated financial information about their reportable segments. In fact, in Forms 10-K and 10-Q, management must analyze the financial performance of the company both as a whole and by segment.



Fair value measurements

Fair value measurements calculated using unobservable inputs are subject to more extensive disclosure requirements than observable inputs. Nonpublic entities may be exempt from some of these requirements, but public companies are not.



Stock options and other forms of share-based compensation

During the IPO process, the SEC staff will require disclosure regarding stock option and other share-based payment awards granted in the periods leading up to the offering. In particular, the disclosures should describe how the company valued these awards. The SEC may challenge cheap stock awards — that is, awards whose value was determined to be significantly lower than the IPO price.



Income taxes

SEC regulations require public companies to reconcile the domestic federal statutory tax rate (that is, 21% in the United States) to the company's effective income tax rate, as shown in its financial statements.



Interest rate swaps

For private companies, the FASB has simplified the accounting for certain interest rate swaps, making it easier to qualify for hedge accounting and measure the value of these derivative instruments. Public companies, however, cannot benefit from this accommodation.



Variable interest entities (VIEs)/consolidation

Private companies may elect a PCC accounting alternative that exempts them from applying the VIE consolidation model to certain common control leasing arrangements. For example, a private company may not have to consolidate a special purpose entity (SPE) set up by the private company's owners for the sole purpose of owning a building that will be leased to the private company. Public companies may not elect a PCC accounting alternative, and therefore have to analyze this same transaction under the complex VIE rules to determine whether the SPE should be consolidated.



Amortizing goodwill from a business combination:

Pursuant to another PCC accounting alternative, private companies are permitted to amortize goodwill from a business combination for a period not to exceed 10 years. Private companies can also elect to perform impairment testing only after a triggering event and at a companywide level. Public companies may not amortize goodwill, and instead must test for impairment annually (or more frequently if impairment indicators exist) at the reporting unit level.



Accounting for intangible assets in a business combination

Following a business combination, public companies must value and report all identifiable assets of the acquired business. Private companies may elect a PCC accounting alternative to forgo recognizing and measuring certain intangible assets such as noncompetition agreements and customer relationships, which can be difficult to value in practice.



New accounting standards

In recent years, the FASB has issued a number of new accounting standards. For many organizations, the new standards could have a significant effect on the entity's financial statements and could require massive changes to internal controls and processes. In terms of ICFR, public companies will have to redesign their existing processes around revenue recognition and evaluate these new controls for purposes of Sarbanes-Oxley Section 404. The new standards also require extensive disclosures, many of which are elective for private companies.





Financial statements of other entities

A company may be required to include in its SEC filings financial statements of other entities, such as significant acquired businesses or equity method investees.

While these entities are often private companies, they are considered public business entities for purposes of financial reporting. Therefore, PCC accounting alternatives cannot be used in preparation of those financial statements.

Again, this discussion outlines only a handful of the potential disparities between private and public company financial reporting. It is critical to consult with your accounting advisers to help identify those differences that are applicable to your organization.

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