California Corporate
& Securities Law

Are Reverse Mergers A Nevada Problem?

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Yesterday, the Securities and Exchange Commission issued this bulletin on the risks of investing in reverse merger companies. In this post from the week before, I wrote about a recent article that found that Nevada is second only to Delaware in attracting out-of-state publicly traded corporations. The article by Professors Michal Barzuza and David C. Smith looked at the number of accounting restatements and found:

> *"Our results suggest that Nevada corporate law attracts a certain class of firms that are prone to financial reporting failures and that these failures are followed by significant losses to shareholder value."*

The article may be downloaded here.

With this article on my mind, I noted that the SEC's bulletin highlighted the fact that in recent months it had suspended trading in six reverse merger entities and I decided to look up where these companies had been incorporated. I found that three of the companies named in the bulletin are incorporated in Nevada, two in Delaware and one in Alberta, Canada.   Although it might be argued that these companies were attracted to Nevada's allegedly lax corporate law, an equally plausible rationale might be that Nevada's fee structure is considerably lower than Delaware.

I did find that EDGAR did not accurately disclose the state of incorporation. For example, the EDGAR filing information for China Changjiang Mining and New Energy Co disclosed that the company is incorporated in Delaware while the company's reports disclose that it is incorporated in Nevada.

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