

## [Securities Regulation Daily Wrap Up, TOP STORY—SEC proposes to streamline debt offering disclosures, \(Jul. 25, 2018\)](#)

Securities Regulation Daily Wrap Up

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The SEC has proposed rule amendments designed to streamline financial disclosure requirements applicable to registered debt offerings for guarantors, issuers of guaranteed securities, and affiliates. The amendments to Regulation S-X Rules 3-10 and 3-16 would focus on the materiality of information in the required disclosures and making them easier for investors to understand, with an eye toward reducing compliance burdens (*Financial Disclosures About Guarantors and Issuers of Guaranteed Securities and Affiliates Whose Securities Collateralize a Registrant's Securities*, [Release No. 33-10526](#), July 24, 2018).

"I have seen firsthand instances in which an issuer did not pursue SEC registration of a debt offering that included a subsidiary guarantee or pledge of affiliate securities as collateral because of the costs and, in particular, time burdens of these rules," [said](#) SEC Chairman Jay Clayton.

**Required disclosures.** A guarantee of a debt security is a separate security under the Securities Act and, as a result, offers and sales of these guarantees must be registered or qualify for an exemption from registration. If the offer and sale is registered, the issuer of the debt security and the guarantor must each file audited annual and unaudited interim financial statements under Regulation S-X. Rule 3-10 requires the filing of financial statements for all issuers and guarantors of registered securities and provides several exceptions, including for individual subsidiaries when a parent company provides certain disclosures in its consolidated financial statements. Rule 3-16 requires a registrant to provide separate financial statements for each affiliate whose securities constitute a substantial portion of the collateral for any class of registered securities as if the affiliate were separately registered.

**Rule 3-10 changes.** Under the proposal, Rule 3-10 would continue to permit the omission of separate financial statements of subsidiaries when the parent company provides supplemental financial and non-financial disclosure about the subsidiary issuers and guarantors and the guarantees. The proposed amendments would, however, replace the condition that a subsidiary issuer or guarantor be 100-percent-owned by the parent company with a condition that it be consolidated in the parent company's financial statements and replace condensed consolidating financial information with disclosures consisting of summarized financial information of issuers and guarantors while reducing the number of periods presented.

In addition, the proposed non-financial disclosures would expand the qualitative disclosures about issuers, guarantors, and guarantees and permit the disclosures to be provided outside the footnotes to the parent company's consolidated financial statements while requiring that the proposed disclosures be included in the footnotes to the parent company's consolidated financial statements for annual and quarterly reports. The proposal would require the disclosures for as long as the issuers and guarantors have an Exchange Act reporting obligation with respect to the guaranteed securities instead of the period during which the guaranteed securities are outstanding.

Proposed Rule 13-01 in new Article 13 of Regulation S-X would specify the disclosure requirements for the accompanying proposed disclosures.

**Rule 3-16 changes.** Under the proposal, the disclosure requirements of Rule 3-16 would be amended and moved to proposed Rule 13-02, and the existing requirement to provide separate financial statements for each affiliate whose securities are pledged as collateral would be replaced with a mandate to provide financial and

non-financial disclosures about the affiliate and the collateral arrangement as a supplement to the consolidated financial statements of the issuer.

In addition, the proposed changes would permit the disclosures to be placed in filings in the same manner as those related to guarantors and guaranteed securities and would replace the requirement to provide disclosure only when the pledged securities reach a certain threshold, with a requirement to provide the disclosures in all cases unless they are immaterial.

According to the SEC, the proposed changes are designed to focus disclosures on information that is material in light of particularized circumstances while making the disclosures easier for investors to understand.

The proposed changes are also intended to reduce compliance costs in order to encourage issuers to offer guaranteed or collateralized securities on a registered basis to increase investor protections and to improve transparency in the market to the extent more offerings are registered. The change may also increase issuers' flexibility to include guarantees or pledges of affiliate securities as collateral when they structure debt offerings, which could lower capital costs, the release explains.

While ultimately supporting the proposal, Commissioner Kara Stein [expressed](#) reservations about the potential for a "slippery slope." She highlighted concerns about the proposal's "increased flexibility" to allow removal of certain information from audited financial statements, noting that this plan could threaten the availability of high-quality financial reporting by providing companies with the "option" of providing material information to investors outside of audited financial statements. "To move away from investor and market accountability, without having a full understanding of the reasons behind doing so, is troubling," she said.

Comments on the proposal are due within 60 days of publication in the *Federal Register*.

The release is [No. 33-10526](#).

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