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Office of the Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-1090

Via email to rule-comments@sec.gov

Re: File No. S7-20-15
Request for Comment on the Effectiveness of
Financial Disclosures about Entities Other than the Registrant

Ladies and Gentlemen:

This letter is submitted on behalf of two committees of the Association of the Bar of the City of New York: the Financial Reporting Committee and the Securities Regulation Committee. Our committees include a wide range of practitioners whose areas of interest and expertise include financial reporting under the securities laws and the regulation of the U.S. capital markets.

We are responding to the request of the Securities and Exchange Commission for comment regarding the financial disclosure requirements in Regulation S-X applicable to certain entities other than the registrant.

Our comments concern Rule 3-05 (Financial Statements of Businesses Acquired or to be Acquired) and Rule 3-10 (Financial Statements of Guarantors and Issuers of Guaranteed Securities Registered or Being Registered).

Rule 3-05

Rule 3-05 currently requires three years of separate audited financial statements for an acquired business if any of the specified significance tests exceeds 50 percent, unless revenues of the acquired business were less than $50 million in its most recent

fiscal year. We would urge the Commission to consider raising the significance threshold for the third year of historical financial statements from 50 percent to 80 percent. Preparing Rule 3-05 financial statements is frequently costly and time consuming for issuers, particularly in instances where financial statements of an acquired business have not previously been audited or prepared in accordance with Regulation S-X. The financial statement requirements can delay the consummation of transactions and in some cases deter them entirely. Moreover, we believe that the third year of historical financial statements is often of limited utility to investors. The Commission has acknowledged as much in other contexts, most recently in adopting rules for "emerging growth companies" ("EGCs") that require only two years of audited financials. In the case of significant acquired businesses, investors are provided with pro forma financial information, which is often more relevant to an investment in the issuer going forward than the historical financial statements of the acquired business, particularly financial statements that are three years old.

For these reasons, we believe the Commission should consider raising the significance threshold for the third year of financial statements from 50 percent to 80 percent, and we note that the 80 percent significance test is already used for purposes of Rule 3-05(b)(4)(iii) as an indicator of "major significance." We also think the Commission could consider eliminating altogether the third year financial statement requirement for any acquired business that would qualify as an EGC if it were the registrant.

Rule 3-10

Rule 3-10 currently provides certain exemptions from the requirement to provide separate audited financial statements for the issuer and the guarantors of registered debt securities. To take advantage of the exemptions, the subsidiary issuers/guarantors must be "100% owned" by the parent company and the guarantees must be "full and unconditional." Under Rule 3-10, in certain fact patterns, a parent company can provide abbreviated narrative disclosure in its financial statements if (i) it has no independent assets or operations and (ii) all of its subsidiaries other than the issuer or guarantor, depending on the fact pattern, are minor. Otherwise, the parent company must provide more detailed condensed consolidating financial information, which can be costly and time consuming to prepare.

We would urge the Commission to consider implementing two changes to Rule 3-10. First, we would recommend replacing the "100% owned" standard with a "wholly owned subsidiary" standard, as defined in Rule 1-02(aa) of Regulation S-X. This would permit reliance on Rule 3-10 where a parent company owns substantially all of a subsidiary's voting shares, but not 100% of the shares, which is the case for companies in jurisdictions where directors are required to own a small number of shares.

Second, we would recommend eliminating the requirement that a parent company have no independent assets or operations as a prerequisite to providing abbreviated narrative disclosure in lieu of the more detailed condensed consolidating information. This would permit a company relying on Rule 3-10 to present narrative disclosure when

the parent has independent assets or operations, as long as all of the subsidiaries outside of the credit group (*i.e.*, subsidiaries other than the issuer or guarantor, depending on the fact pattern) are minor. Under the current rules, we believe the costs of preparing condensed consolidating information outweigh the benefits to investors where a parent has some independent assets or operations but all of the entities outside the credit group are minor.

In addition, we believe it would be beneficial to investors and issuers if the Commission were to codify in Rule 3-10 the staff guidance regarding customary circumstances for release of a subsidiary's guarantee that would permit continued reliance on Rule 3-10, which guidance is currently set forth in the Financial Reporting Manual of the Division of Corporation Finance.

We thank you for the opportunity to comment on this important Commission initiative to revisit the effectiveness of financial disclosures about entities other than the registrant. Members of our committees would be happy to discuss any aspect of this letter with the Commission staff.

Respectfully submitted,

David S. Huntington, Chair
Financial Reporting Committee

Marc M. Rossell, Chair
Securities Regulation Committee