

July 6, 2017

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

Re: Request for Comment, “Possible Changes in Industry Guide 3,” File No. S7-02-17

Dear Office of the Secretary:

Crowe Horwath LLP (“Crowe” or “we”) appreciates the opportunity to provide our input on the SEC’s Request for Comment, “Possible Changes to Industry Guide 3” (“Request”). We commend the SEC on its efforts to help improve registrant’s disclosures and holistically review the financial and other information provided by registrants to investors, including its broader initiative on Disclosure Effectiveness.

Crowe audits more than 100 domestic issuers, more than 60 of which are financial institutions, and it is from this perspective that we provide our commentary.

Overview

Guide 3 was first published in 1976 and last updated in 1986. In the intervening three decades, generally accepted accounting principles (GAAP) and the depth and breadth of business practices of financial institutions have changed significantly. As auditors, we offer feedback on topics such as the applicability and scope of Guide 3 as well as whether certain disclosure requirements are duplicative of or meet the same disclosure objective of GAAP or have become less relevant due to changes in the business environment.

Further, we encourage the SEC to continue its outreach to investors, preparers, and other constituency groups, as they are best suited to provide input on various other topics such as the cost and burdens involved in preparing Guide 3 disclosures, whether current Guide 3 disclosures remain useful, and whether additional disclosures not currently called for in Guide 3 would be useful to investors and other stakeholders.

Applicability and Status of Industry Guide 3, “Statistical Disclosure by Bank Holding Companies” (Guide 3)

Guide 3’s preface indicates it applies to “bank holding companies;” however, the staff of the SEC’s Division of Corporation Finance and Office of the Chief Accountant (collectively, the Staff) have more broadly interpreted the applicability of Guide 3. In Staff Accounting Bulletin Topic 11:K, the Staff indicates “to the extent particular guidance [in Guide 3] is relevant and material to the operations of an entity, the [S]taff believes the specified information, or comparable data, should be provided.” Staff Accounting Bulletins are interpretations of the Staff and are “not legally binding,”¹ and we have observed that some

¹ <https://www.sec.gov/interps.shtml>

non-bank holding company registrants are uncertain about whether Guide 3 is applicable to their operations.

Uncertainty with respect to the applicability of Guide 3 to a non-bank holding company can impede capital formation because a registrant might incur costs to prepare Guide 3 disclosures when the disclosure is not required or the Staff might request a registrant to add Guide 3 disclosure during the registration process when the registrant otherwise believed the disclosure was not required. We recommend the Commission clearly define the applicability of Guide 3 so non-bank holding company registrants can make consistent judgments with respect to providing the disclosures recommended by Guide 3.

Guide 3 is currently not a Commission rule nor does it bear the Commission's official approval.² For the reasons noted in our previous comment letter³ to the Commission's Concept Release on "Business and Financial Disclosure Required by Regulation S-K," we recommend the Commission codify Guide 3 as an approved Commission rule.

Periods Required Under Guide 3

Unless a registrant is below certain quantitative thresholds,⁴ Guide 3 currently requires five years of loan portfolio and summary of loan loss experience data and three years of data for all other requested data. In most cases, the data provided pursuant to Guide 3 will exceed the number of periods of financial statements presented by a registrant in its filing. We encourage the staff to reconsider this requirement.

In a registration statement, entities that have generally been afforded certain disclosure accommodations, including Smaller Reporting Companies ("SRCs"), Emerging Growth Companies ("EGCs"), and non-issuer targets in a Form S-4 registration statement, often have to prepare Guide 3 data that exceeds the periods of its basic financial statements presented in the filing. The requirement to provide statistical data for years prior to the periods covered by the basic financial statements can be burdensome, in particular for the aforementioned types of entities, when the entity has not previously prepared similar data.

Additionally, in the case of EGCs, the provision of statistical data for periods prior to the basic financial statements in an EGCs IPO registration statement might be viewed as inconsistent with the Staff's other interpretive positions on EGC disclosures. In this regard, we note the Staff has clarified that certain disclosures (for example, selected financial data) need not be provided for periods prior to the earliest period presented in an EGC's IPO registration statement.

The Commission's Concept Release on "Business and Financial Disclosures Required by Regulation S-K"⁵ notes that most investors, even those who rely on financial advisors, use the Internet to conduct transactions and gather financial information. For registrants who currently file periodic reports, we question whether the requirement to provide Guide 3 data beyond the periods presented in the basic financial statements has been rendered obsolete by investors' ability to quickly access, manipulate, and analyze data using the Internet.

To the extent the SEC determines to keep the currently specified periods in place, we encourage the SEC further scale Guide 3 requirements for SRCs, EGCs, and, in an S-4 registration statement, non-issuer targets by not requiring statistical data beyond the periods shown in the basic financial statements.

Disclosure Framework of Guide 3

Guide 3 is rules-based, prescriptive, and includes a number of bright-line quantitative tests that trigger disclosure. Guide 3 currently allows for presentation of the required statistical data in either the business

² 41 FR 39007

³ <https://www.sec.gov/comments/s7-06-16/s70616-279.pdf>

⁴ Less than \$200 million in total assets or less than \$10 million of equity, as defined in General Instruction 3(c) of Guide 3

⁵ <https://www.sec.gov/rules/concept/2016/33-10064.pdf>

section of a filing or in Management's Discussion and Analysis ("MD&A") "if in management's opinion such presentation would be more meaningful to investors."⁶ MD&A, as noted in the Staff's 2003 interpretive release,⁷ is an objective oriented disclosure rule, and its intent is to "be a discussion and analysis of a company's business as seen through the eyes of those who manage that business. Management has a unique perspective on its business that only it can present."⁸

There is an inherent conflict between the current prescriptive and bright-line quantitative disclosure triggers in Guide 3 and the option for preparers to present Guide 3 information in a section of the filing whose stated objective is to provide entity specific and tailored information that communicates how management views the business. In addition, the Guide 3 adopting release in 1976 noted "as the operations of bank holding companies have diversified, it has become increasingly difficult for investors to identify the sources of income of such companies,"⁹ and the Guide therefore calls for more meaningful disclosure about, among other items, loan portfolios. As noted in the aforementioned MD&A interpretive release, meaningful disclosure is fostered when management has flexibility in how it achieves a disclosure objective.

We encourage the SEC to consider whether Guide 3 should be revised to identify specific disclosure objectives in contrast to its current prescriptive and bright-line approach. Such an approach would be consistent with the Staff's conclusions in its "Study Pursuant to Section 108(d) of the Sarbanes-Oxley Act of 2002 on the Adoption by the United States Financial Reporting System of a Principles-Based Accounting System"¹⁰ ("Study"). While the Study was written primarily from the perspective of accounting standard setting, its message that an objective oriented regime "creates an incentive for good companies to be more forthcoming in providing clear and transparent information to investors...[and] result[s] in information that is more understandable (and, hence, more useful) to investors." Stating a disclosure objective and allowing management the flexibility to meet the disclosure objective in a manner that reflects how it views their business would provide meaningful and decision useful information to users.

Providing management the flexibility to use its view of the business when drafting disclosures pursuant to Guide 3 would be consistent with the expectations of various stakeholders with respect to financial institutions' implementation of the FASBs recent standard on credit losses.¹¹ The credit loss standard will require significant implementation effort on the part of financial institutions, and various stakeholders have acknowledged that a financial institution's implementation should not be a "one-size fits all approach,"¹² rather, a financial institution's approach should be tailored to its specific facts and circumstances. Likewise, preparers should also be afforded flexibility in their Guide 3 disclosures when the new credit loss standard is effective.

Disclosure Overlap with US GAAP and SEC Rules

Since the last substantive update of Guide 3 in 1986, GAAP has changed considerably, and many of the disclosure requirements of Guide 3 have since been included in GAAP. In addition, certain Guide 3 disclosures overlap with SEC rules that require similar disclosures in a registrant's financial statements. For example, while not an exhaustive list, the following table demonstrates the overlap between Guide 3 and a) specific GAAP disclosures or the disclosure objective of the relevant GAAP; and b) SEC Rules:

⁶ General Instruction 2 of Guide 3

⁷ Release No. 33-8350

⁸ Ibid.

⁹ 41 FR 39008

¹⁰ <https://www.sec.gov/news/studies/principlesbasedstand.htm>

¹¹ Accounting Standards Update 2016-13: Financial Instruments - Credit Losses (Topic 326)

¹² See for example, <https://www.sec.gov/news/speech/bricker-remarks-aicpa-national-conf-banks-savings-institutions.html>

Guide 3 Section	GAAP Topic or SEC Rule
Section II, Investment Portfolio	ASC 320 – Investments – Debt and Equity Securities
Section III and IV, Loan Portfolio and Summary of Loan Loss Experience	ASC 310 - Receivables (and ASC 326 – Credit Losses, when adopted)
Section V, Deposits, Subsection D	ASC 942 – Financial Services – Depository and Lending
Section VII, Short Term Borrowings, Subpoint 1	Article 9 of Regulation S-X

As a result of the overlap between Guide 3 and GAAP and SEC Rules, entities often must prepare disclosure outside the audited financial statements pursuant to Guide 3 that are redundant with disclosures included inside the financial statements pursuant to GAAP and SEC Rules. They must prepare two separate sets of disclosures because the format and presentation of the duplicative information at times differs. As noted in our comment letter¹³ to the SEC’s Disclosure Update and Simplification proposal, the SEC has designated the Financial Accounting Standards Board (“FASB”) as the private-sector accounting standard setter for U.S. financial reporting purposes, and we submit the disclosures resulting from the FASB’s due process should be sufficient for investors and other users of financial statements to make informed investment decisions. To the extent GAAP or other SEC required financial statement disclosures are redundant with Guide 3 in content or objective, we encourage the SEC to consider removing the related Guide 3 disclosure requirement.

Certain disclosure requirements of Guide 3 are not duplicative with GAAP or SEC rules (for example, Section I, Section VI, and certain portions of Section V and VII). However, should the SEC elect to pursue an objective oriented disclosure approach, we suggest the SEC seek ways to incorporate the aforementioned incremental Guide 3 disclosures into MD&A, which, as stated in various Staff releases (for example, Release 33-8350) is currently an objective based disclosure rule. As an illustration, Item I of Guide 3 helps to explain variances in key revenue metrics, which is consistent with MD&A’s objective to analyze and identify trends in an entity’s results of operations.

Potential New Disclosures

The Request outlines areas where Guide 3 might be expanded to provide new disclosures about registrant activities not currently covered by Guide 3. We recommend the SEC only propose new disclosure after conducting significant outreach to investors and preparers. Moreover, consistent with our prior statements regarding an objective oriented Guide 3 disclosures, we encourage the SEC to carefully consider whether the intended disclosure objective of any proposed new disclosure is duplicative of current GAAP or issued but not yet effective accounting standards updates. For example, the Request states “[we] are considering whether to expand Guide 3 to include disclosures on non-interest income activities,” including disaggregated revenue disclosures. Topic 606, however, appears to meet a similar disclosure objective (that is, disaggregation of revenue streams in a decision useful manner).

Through this comment letter process, additional new disclosures not required by GAAP or SEC rules might be suggested. We acknowledge the SEC has a mission that differs from the objectives of the FASB and additional incremental disclosures outside of the financial statements pursuant to Guide III might be appropriate. However, to the extent the SEC considers adding new disclosures to Guide III requirements, we encourage the SEC, as part of its rule-making due diligence, to conduct additional outreach to determine if the FASB has ever considered similar disclosure in any previous standard setting and if so, to understand why such new disclosure was not incorporated into GAAP.

¹³ <https://www.sec.gov/comments/s7-15-16/s71516-40.pdf>

Hyperlinks to Regulatory Filings

The Request asks whether the SEC should require hyperlinks directly to regulatory filings contained on an external website (for example, Call Reports) or incorporate by reference such information into a registrant's filing. We support the SEC's endeavors to streamline registrant reporting, and the use of external hyperlinks or incorporation by reference can be an effective means to efficiently communicate information to investors and other users. However, we also observe there are several potential issues with such an approach.

Hyperlinks pose a particular challenge to auditors fulfilling their responsibility under PCAOB AS 2710 "Other Information in Documents Containing Audited Financial Statements." Requiring registrants to hyperlink to external websites has the potential to raise questions as to what constitutes the "document" for the purposes of fulfilling our professional obligation under PCAOB AS 2710. We have similar concerns with respect to our Section 11 liability in a Securities Act Registration Statement under PCAOB AS 4101 "Responsibilities Regarding Filings Under Federal Securities Statutes."

Call Reports and other regulatory filings might not be prepared at the same reporting entity level or using the same presentation basis as depicted in its financial statements in its SEC filings. For example, an entity's Call Report might be prepared at the level of an individual bank whereas the consolidated entity's SEC filing might be prepared at a holding company level. In addition, the Call Report instructions might require certain presentations that are different and/or more disaggregated than in an SEC filing. Finally, disclosure in a SEC registrant's filing has a significantly different objective than the same entity's disclosure for its Call Report, which is focused on providing disclosure for safety and soundness purposes rather than disclosure for investors. For these reasons, requiring hyperlinks or incorporating Call Report information into SEC filings has the potential to cause investor confusion. Should the SEC continue down a path of requiring hyperlinks to regulatory reports or incorporating such information by reference, we encourage additional outreach to the PCAOB and users of the financial statements to address our concerns, and we suggest the SEC clarify how an auditor's Section 11 liability would be impacted.

Closing

We appreciate the opportunity to express our views on questions raised in the Request. Please contact Brad A. Davidson at [REDACTED] or Mark C. Shannon at [REDACTED] to answer any questions regarding the views expressed in this letter.

Sincerely,



Crowe Horwath LLP