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July 29, 2019

U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090
Attention: Vanessa Countryman, Secretary

Re: Amendments to Financial Disclosures about Acquired and Disposed Businesses
File Number S7-05-19

Dear Ms. Countryman,

We appreciate the opportunity to submit this letter to the Securities and Exchange Commission (the "Commission") on the proposed amendments to the financial disclosure requirements for acquired and disposed businesses (Release No. 33-10635; 34-85765; IC-33465; File No. S7-05-19) (the "Proposal").

We support the Commission's efforts to improve the quality of financial information provided to investors, facilitate more timely access to capital and reduce the burden on registrants in preparing the required financial disclosures. However, we believe aspects of the proposed amendments should be modified to enhance the Commission's efforts. In this letter, we identify a number of enhancements to the Proposal that we believe are consistent with the Commission's underlying policy objectives.

Non-Applicability of Proposed Amendments to Proxy Statements and Registration Statements on Form S-4 / F-4

The proposed amendments would result in significant changes to the financial disclosure requirements in Rule 3-05 and Article 11 of Regulation S-X, among other changes. Consequently, a registrant seeking to sell securities pursuant to a registration statement on Form S-1 or S-3 (the financial statement requirements of which are cross-referenced directly to Rule 3-05 and Article 11 of Regulation S-X) would be able to avail itself of the abbreviated disclosure requirements offered by the proposed amendments. However, Footnote 6 of the Proposal states that "the proposed amendments would not apply to financial statements related to the acquisition of a business that is the subject of a proxy statement or registration statement on Form S-4 or Form F-4." Although Footnote 6 clarifies that financial information required in such filings provided pursuant to Rule 3-05 and Article 11 of Regulation S-X would be subject to the proposed amendments, certain transactions which are disclosed pursuant to a filing of a proxy statement or registration statement on Form S-4 or F-4 would not benefit from the proposed amendments, because the underlying disclosure requirements are built into the applicable rules and not made by cross-reference to Rule 3-05 and Article 11 of Regulation S-X. For example, where the company being acquired is a non-reporting entity under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and the registrant's security holders are voting in the transaction, the parties must provide consolidated and audited balance sheets of the acquired company as of the end of the two most recent fiscal years and audited statements of income and cash flows for each of the three most recent fiscal years.[1]

The Commission should consider the negative impact that not extending corresponding amendments to Forms S-4 and F-4[2] may have on the ability of public companies to raise capital in connection with an acquisition. To obtain financing for acquisitions, public companies often raise capital through securities offerings, both registered and unregistered. In the context of a registered offering, under the Proposal, the financial statements required would be impacted by the proposed amendments and would consequently be less than what would be required in connection with an acquisition subject to a proxy statement or registration statement on Form S-4 or F-4. In the context of an unregistered offering, such as an offering under Rule 144A under the Securities Act of 1933, as amended (the "Securities Act"), the form and content of the offering documentation in such transactions is not subject to review by the Staff of the Commission. Offering participants therefore have flexibility to negotiate the extent to which financial statement disclosure is provided and will frequently reach a consensus on an approach that provides investors with all material financial statement information – but omit information that is not material and which is unfairly burdensome to the issuer. Clearly, these decisions going forward will be informed by changes to Item 3-05 and Article 11 of Regulation S-X made by the Proposal.

If, however, such changes under the Proposal are not extended to Forms S-4 and F-4, we are concerned that the different requirements could cause uncertainty in the acquisition financing markets regarding financial statement requirements and result in possible delays. Also, participants in acquisition financing transactions may feel compelled to include in offering documentation financial statements required under Form S-4 or F-4 (but which would otherwise not be required by, for example, Forms S-1 or S-3 if the Proposal were adopted in its current form) in situations where the acquirer will be required to file a proxy statement or registration statement on Form S-4 or F-4 in connection with the acquisition. This would be particularly problematic in the context of a registered offering, where offering participants may be reluctant to incur potential liability under Section 11 of the Securities Act by issuing securities when additional periods of financial statements will be forthcoming in connection with the filing of a proxy statement or registration statement on Form S-4 or F-4. We are concerned that this result could cause uncertainty in the acquisition financing market and lead to delays in the timing of such financing transactions, as well as incremental costs for issuers.

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1 *See* Form S-4, Item 17(b)(7), citing Rule 14a-3 under the Exchange Act.

2 We do not believe changes to Schedule 14A are necessary, as the applicable financial statement requirements under Schedule 14A are made by cross-reference to Form S-4 or Form F-4, as applicable. *See* Schedule 14A, Item 14(c).

We believe the Commission's desire in the Proposal to strike an even balance between investors' desire for useful financial information and the burden on registrants in providing such information should apply similarly to transactions that are the subject of a proxy statement or registration statement on Form S-4 or F-4. If not addressed, the lack of change to the acquired company disclosure requirements under Forms S-4 and F-4 has the potential to impair or delay financing in M&A transactions, both by putting registrants at a disadvantage when considering and structuring an acquisition and by impeding the capital raising process that is frequently undertaken in connection with an acquisition. We respectfully suggest that the final rulemaking address the financial disclosure rules applicable to Forms S-4 and F-4 in a manner consistent with the Proposal.

Management's Adjustments

We note that the Proposal aims to improve the quality of pro forma financial information delivered to investors through a proposed requirement to require both "Transaction Accounting Adjustments" and "Management's Adjustments" in connection with Regulation S-X Article 11 pro forma financial statements.[3] Although we are generally supportive of the Commission's goal of providing higher quality information to investors, we believe that the requirements related to Management's Adjustments, as proposed, may result in unintended adverse consequences.

Under the Proposal, registrants will be required to include line item adjustments in a new Management's Adjustments column for synergies and other transaction effects. The requirement to include synergy adjustments creates potential liability for the registrant with respect to such adjustments as synergies are based on inherently uncertain information, and management will be required to exercise a significant level of judgment in providing this information. We expect that these adjustments will be of particular sensitivity to auditors and underwriters in the context of securities offerings, and transaction parties will therefore be required to devote potentially significantly increased time and resources in conducting diligence with respect to the synergy adjustments. It is unclear to us whether the benefit of providing this information outweighs the increased costs associated with doing so. We therefore invite the Commission to address the potential for liability with respect to Management's Adjustments in its final rulemaking. To this end, we support the proposed application of the forward-looking information safe harbors under Securities Act Rule 175 and Exchange Act Rule 3b-6 to Management's Adjustments.

We also ask the Commission to propose a standardized cut-off point, or "realization period," by which synergies must be realized. Under the proposed amendments, in order to be included, Management's Adjustments must be reasonably estimable and have occurred or be reasonably expected to occur. Although these criteria are sufficient to prevent the inclusion of improper adjustments, we nonetheless expect that underwriters and the investing community will seek to impose a realization period with respect to the presentation of synergies. We therefore recommend the Commission adopt a realization period of 18–24 months, as this length will be sufficient to capture the majority of qualifying synergies and is consistent with the market standard under modern leveraged lending practice. Under a standard leveraged credit facility, for

3 *See* Proposal, Section II.D.1.

example, the borrower often is required to comply with one or more financial covenants calculated using an "Adjusted EBITDA" or similar measure. Under the contractually negotiated definition of such measures, the borrower is customarily able to include "add-backs" for non-recurring items, including transaction synergies and "run rate" cost-savings expected to be realized within a specified period, to calculate Adjusted EBITDA and, therefore, its compliance with any financial covenants that use such a measure. By adopting a realization period in its final rulemaking, the Commission can limit potential confusion and conflict among market participants.

Finally, we recommend that the Commission consider clarifying or deleting the proposed standard that any Management's Adjustments reflect only those synergies and other transaction effects which are "reasonably estimable," as we believe the adoption of this standard may create confusion and additional cost for registrants. We believe that the remaining criteria for including adjustments giving effect to synergies and other transaction effects (*i.e.*, that such synergies or effects "have occurred or are reasonably expected to occur") are sufficient to prevent the inclusion of unrealistic synergy adjustments. In the context of financial disclosure, the standard of "reasonably estimable" is commonly associated with Accounting Standard Codification No. 450 ("ASC 450") and accounting for contingencies. The Proposal does not make clear whether the "reasonably estimable" standard for Management's Adjustments is intended to incorporate or otherwise tie to the ASC 450 standard. We do not believe that this is the intent and therefore invite the Commission to clarify how the "reasonably estimable" standard should be evaluated or, alternatively, strike the reference entirely. Absent this clarification, we are concerned that issuers and other market participants will mistakenly infer principles under ASC 450 when assessing whether individual Management's Adjustments must be included.

<u>Financial Statements for Net Assets that Constitute a Business</u>

We acknowledge and support the Commission's attempt to provide relief for registrants acquiring components of an entity, such as a product line or line of business contained in more than one subsidiary of the selling entity.[4] Recognizing the burden that registrants face in preparing full financial statements in connection with the acquisition of a component of an entity that nonetheless qualifies as a "business" under Rule 11-01(d) of Regulation S-X, the Proposal contemplates allowing the registrant to provide abbreviated financial statements in connection with the acquisition of a components of entities, subject to the satisfaction of several conditions, including that preparing full Rule 3-05 financial statements is "impracticable." We invite the Commission to consider whether the "impracticable" standard is necessary for the final rule. We note that the other conditions which must be met before allowing abbreviated financial statements are based on factual matters, such as whether separate financial statements have previously been prepared for the acquired component or whether the seller has maintained distinct and separate accounts which would enable the preparation of full financial statements. Each of these fact-based conditions support the argument that preparing full financial statements that would otherwise be required under Rule 3-05 would be difficult and burdensome on the

4 *See* Proposal, Section II.A.3.

registrant. Thus, if each of these conditions is met, proposed Rule 3-05(e) will be sufficient to prevent abuse without the "impracticable" standard. Including an impracticability requirement, however, adds an element of subjective judgment that would appear unnecessary to achieve the Commission's goals. We therefore ask the Commission to consider striking the impracticability standard in favor of relying strictly on the fact-based conditions specified in the remainder of proposed rule.

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As noted above, we support the Commission's efforts to improve the quality of financial information provided to investors, facilitate more timely access to capital and reduce the burden on registrants in preparing the required financial disclosures. If it would be helpful to discuss this letter or our views of the Proposal otherwise, please do not hesitate to call Paul M. Rodel at [redacted].

Respectfully submitted,

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