



November 30, 2015

Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

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Re: File Number S7-20-15

RSM US LLP appreciates the opportunity to offer our comments on SEC Release No. 33-9929, *Request for Comment on the Effectiveness of Financial Disclosures about Entities Other Than the Registrant*. RSM US LLP is a registered public accounting firm serving middle-market issuers, brokers and dealers.

We support effective financial disclosures that better enable investors to make well-informed decisions about their investments. We therefore support the Commission's efforts to review Regulation S-X, and its decision to initially review the discrete, but important, subset of Regulation S-X disclosure requirements applicable to entities other than the registrant. We understand that investors will provide their views to the Commission regarding the financial disclosures that are important to them. Our views expressed in this letter are based on our experience in working with registrants as well as private companies whose financial statements are required to be included in filings with the SEC.

Our comments focus on issues we most frequently observe our clients encountering when complying with:

- S-X Rule 1-02(w), *Significant subsidiary definition and test*
- S-X Rule 3-05, *Financial statements of businesses acquired or to be acquired*
- S-X Rule 3-09, *Separate financial statements of subsidiaries not consolidated and 50 percent or less owned persons*
- S-X Rule 3-10(g), *Recently acquired subsidiary issuers or subsidiary guarantors*

S-X Rule 1-02(w), Significant subsidiary definition and test

The investment, asset and income significance tests defined in S-X Rule 1-02(w) are used in various SEC rules and regulations to determine whether financial statements of entities other than the registrant, such as acquired companies under S-X Rule 3-05 and equity-method investees under S-X Rule 3-09, must be included in SEC filings. We believe the investment, asset and income tests as currently set forth in Rule 1-02(w) can be challenging to apply and also can result in the provision of financial statements that may not be material to investors.

Investment and asset tests under S-X Rule 1-02(w)

The investment and asset tests are primarily based on carrying amounts, which may not necessarily reflect the significance of the tested entity to the registrant. Also, the investment test calculation compares fair value (e.g., consideration paid for the investment) to carrying value (e.g., total assets of the registrant), which may not result in a meaningful determination of the significance of the tested entity to the registrant. Therefore, as another alternative to the existing investment and asset tests we suggest a

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fair value test, which would compare the fair value of the registrant's investment in the tested entity (i.e., consideration transferred for purposes of Rule 3-05 or equity-method investment for purposes of Rule 3-09 or 4-08(g)) to the fair value of the registrant with a readily determinable market capitalization.

Income test under S-X Rule 1-02(w)

Our clients have encountered circumstances in which the application of the Rule 1-02(w) income test resulted in the requirement to provide financial statements that they believed were not material to investors (or the need to seek waivers to omit such financial statements). This is particularly true in situations where a parent company has near-breakeven income or loss and the recently acquired company or equity-method investee has income in the period tested. The requirement to provide financial statements, which may not be considered to be material, in these circumstances also has ongoing cost consequences because future registration statements will require the consent of the auditor of the acquired entity or equity-method investee for any periods for which the auditor issued an audit opinion.

Because the Rule 1-02(w) income test can result in the requirement to provide financial statements that may not be material to investors, we recommend the Commission consider the use of revenues as the metric, instead of income (i.e., compare the registrant's proportionate share of net revenues of the tested entity to the registrant's consolidated net revenues for the most recently completed fiscal year).

As noted above, in situations in which the parent company has near-breakeven income or loss, the income test can result in the requirement to provide financial statements that may not be material to investors. Therefore, if the income test is retained, we recommend amending the calculation of average income for the registrant to allow either (a) excluding loss years from the denominator, or (b) utilizing the absolute value of loss years in the calculation.

S-X Rule 3-05, *Financial statements of businesses acquired or to be acquired*

We have encountered situations in which our clients could not comply, or had difficulty complying, with the provisions of S-X Rule 3-05 because the required audited financial statements were not obtainable (e.g., acquisitions of entities in bankruptcy) or not readily available for all required periods. Therefore, in addition to our suggestions above for revising the significance test under Rule 1-02(w), we offer the following recommendations for potential changes or alternatives to the disclosure requirements in Rule 3-05.

Two years of audited financial statements

We recommend that the Commission require no more than two years of audited financial statements for acquisitions, except in limited circumstances such as predecessors or reverse acquisitions. Such a revision would parallel the requirement for emerging growth companies and smaller reporting companies conducting initial public offerings (IPOs) to provide only two years of audited financial statements for the registrant and its acquired business.

Accommodation to accept private company alternatives in S-X Rule 3-05 financial statements

The Financial Accounting Standards Board has issued accounting standards with simplified alternatives for the way private companies account for certain matters, such as goodwill, certain interest rate swaps, common control leases and certain intangible assets (private company alternatives). These steps have helped many private companies save both money and time without compromising the relevance and usefulness of the information included in their financial statements.

However, if a private company that elected such private company alternatives is required to apply the provisions of Rule 3-05, it would qualify as a public business entity under U.S. GAAP and would need to

retrospectively reverse its application of the private company alternatives for all periods presented. This complicates the decision around whether the accounting alternatives are viable options for private companies, including family-owned businesses that may possibly be acquired by a registrant in the future. Such companies must decide to either continue using the existing guidance with its known costs and complexity or elect the accounting alternatives, knowing that any future filings with the SEC will come with the incurred cost of retrospectively applying the existing guidance.

We don't believe the potential benefits outweigh the costs of requiring a private company that has applied the private company accounting alternatives to retrospectively reverse them in these situations. Further, the mere potential of incurring costs to retrospectively adjust financial statements could keep private companies from taking advantage of the reduced complexity and financial reporting costs provided by the accounting alternatives. We therefore encourage the Commission work with the FASB to provide an accommodation to allow private company alternatives in financial statements required by Rule 3-05, provided adequate disclosure is made of the differences between the accounting principles used in preparing the Rule 3-05 financial statements and those used under U.S. GAAP for public business entities.

Compliance with Regulation S-X requirements and SEC staff accounting positions

In addition to the costs involved with preparing financial statements under U.S. GAAP for public business entities, further incremental costs are incurred and additional time is needed to ensure that an acquired private company's financial statements comply with the requirements of S-X Articles 4 and 5 as well as Staff Accounting Bulletins and Emerging Issues Task Force Observer comments. We recommend the Commission also weigh the benefits of these requirements with the incremental costs and potential filing delays necessary to comply with these requirements.

Use of abbreviated financial statements

When full financial statements are not obtainable or readily available, as noted above, we recommend the Commission allow the use of abbreviated financial statements (e.g., statements of revenue and direct expenses and a statement of assets acquired and liabilities assumed) if the registrant also provides disclosures they believe appropriately inform investors about the acquired business.

Investment company considerations

Many times when investment companies, particularly business development companies (BDCs), are formed through the acquisition of investment funds or a significant portion of the assets of investment funds, the investment company may have limited historical information in its IPO registration statement. Therefore, when evaluating the significance of investment funds acquired by investment companies, we recommend the test for significance being based on the pro forma results of the registrant. Also, we believe an audited schedule of investments would provide the appropriate information for prospective investors to understand the likely composition of a newly formed investment company. Therefore, we suggest the Commission consider whether an audited schedule of investments would suffice in lieu of audited financial statements of an acquired investment fund for investment company IPOs.

S-X Rule 3-09, *Separate financial statements of subsidiaries not consolidated and 50 percent or less owned persons*

We have observed situations in which our clients have encountered the following challenges in applying the provisions of S-X Rule 3-09:

- Low levels of ownership interest by the registrant or other involvement with the investee limiting the ability of the registrant to easily obtain audited investee financial statements
- Difficulty obtaining the required financial statements and having them audited in a short period of time in situations where the registrant was not able to determine investee significance until after year end primarily due to the application of the income test discussed above

To reduce situations in which financial statements would be required by Rule 3-09, we suggest amending Rule 3-09 to increase the threshold for significance to only require separate financial statements when the investee is so significant that financial information that otherwise would be provided by S-X Rule 4-08 (g) does not provide sufficient information for investors to understand the consolidated results and financial condition of the registrant. We also suggest amending Rule 3-09 so as to only require financial statements for years in which the significance tests are met.

Also, we believe more relevant information could be provided if Rule 4-08(g) were revised as follows:

- For each investee that is individually significant, require summarized financial information to be presented separately. Such information could be better understood if presented in a columnar format that reconciles the investees' net assets and net income to the consolidated financial statements.
- Eliminate the current requirement to present combined summarized financial information of investees when they exceed 10% significance in the aggregate. As an alternative to this requirement, consider narrative disclosures that would provide more useful information.

Further, there is some confusion in practice as to whether Rules 3-09 and 4-08(g) apply to investment companies. If the Commission concludes that financial information for significant investees of investment companies should be required, we recommend the following revisions:

- For purposes of the significance test:
 - Only require financial statements for investees that exist as of the reporting date
 - In the income test, replace "income" with:
 - Investment income earned by a BDC from the investee for the numerator
 - Total consolidated investment income earned by the BDC for the denominator
- Consider whether the inclusion of separate financial statements of investee portfolio companies is necessary under most circumstances for BDCs. If the Commission believes Rule 3-09 and 4-08(g) financial information is needed, in lieu of separate financial statements, we recommend the provision of certain summarized information (which may include a schedule of investments for an investment company investee) for each significant investee with no aggregation.

S-X Rule 3-10(g), *Recently acquired subsidiary issuers or subsidiary guarantors*

Compliance with the reporting requirements of S-X Rule 3-10(g) can be costly and difficult for a recently acquired company that becomes a guarantor of a registrant's debt. Therefore, if financial information is required by Rule 3-10(g) for newly acquired guarantor subsidiaries, we suggest allowing registrants to use the same significance testing metrics discussed above for acquired businesses (by comparison of the acquired guarantor subsidiary to the guarantors and issuer combined) instead of the current test involving the principal amount of the securities being registered. Also, the newly acquired guarantor or issuer subsidiary's financial statements should not be required to comply with public company form and content.

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Further, such financial statements should not be required to be audited in accordance with the standards of the Public Company Accounting Oversight Board (PCAOB) if the financial statements already have been audited in accordance with U.S. generally accepted auditing standards. Conducting an audit in accordance with the standards of the PCAOB requires the application of the PCAOB and SEC auditor independence rules. There could be situations in which an auditor is independent with respect to its private company audit client under the auditor independence rules of the American Institute of Certified Public Accountants, but is not independent under the PCAOB or SEC auditor independence rules and therefore is precluded from performing an audit in accordance with PCAOB standards. This situation could require the financial statements to be re-audited by another registered public accounting firm, thus resulting in substantial incremental costs for the recently acquired company.

We would be pleased to respond to any questions the Commission or its staff may have about our comments. Please direct any questions to Scott Pohlman, National Director of SEC Services, at

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Sincerely,

RSM US LLP

RSM US LLP