

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 210, 211, 228, 240 and 249

[Release Nos. 33-7878; 34-43124; International Series No. 1229; FR-55; File No. S7-7-99]

RIN 3235-AH52

Financial Statements and Periodic Reports for Related Issuers and Guarantors

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: We are adopting financial reporting rules for related issuers and guarantors of guaranteed securities. We also are adopting an exemption from Exchange Act periodic reporting for subsidiary issuers and subsidiary guarantors of these securities. These rules codify, in large part, the positions the staff has developed through Staff Accounting Bulletin No. 53, later interpretations, and the registration statement review process. We intend for these rules to eliminate uncertainty about which financial statements and periodic reports subsidiary issuers and subsidiary guarantors must file. We also intend these rules and the guidance we provide in this release to eliminate substantially the need for requests for staff "no-action" letters in this area.

EFFECTIVE DATE: September 25, 2000, except that Form 20-F (referenced in § 249.220f) is effective September 30, 2000.

FOR FURTHER INFORMATION CONTACT: Regarding Rule 12h-5, Michael Hyatte at (202) 942-2900; regarding the Regulation S-X and Regulation S-B revisions, Craig Olinger at (202) 942-2960, both in the Division of Corporation Finance.

SUPPLEMENTARY INFORMATION: We are adopting amendments to Rule 3-10¹ of Regulation S-X² and Item 310³ of Regulation S-B.⁴ We are adopting new Rule 3-16⁵ of Regulation S-X and new Rule 12h-5⁶ under the Securities Exchange Act of 1934.⁷ We are amending Form 20-F⁸ under the

Exchange Act. We also are rescinding Staff Accounting Bulletin No. 53.⁹

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I. Executive Summary

Over the past two decades, it has become increasingly common for a parent company to raise capital through:

- Offerings of its own securities that are guaranteed by one or more of its subsidiaries; and
- Offerings of securities by a subsidiary that are guaranteed by the

¹ 17 CFR 210.3-10.

² 17 CFR 210.1-01 through 12-29.

³ 17 CFR 228.310.

⁴ 17 CFR 228.10 through 702.

⁵ 17 CFR 210.3-16.

⁶ 17 CFR 240.12h-5.

⁷ 15 U.S.C. 78a *et seq.*

⁸ 17 CFR 249.220f.

⁹ Staff Accounting Bulletin Release No. SAB 53 (June 13, 1983) [48 FR 28230].

parent company and, sometimes, one or more of the parent company's other subsidiaries.

Guarantees of securities are securities themselves for purposes of the Securities Act of 1933.¹⁰ As a result, the Securities Act requires the offering of both the guaranteed security and the guarantee to be either registered or exempt from registration. A Securities Act registration statement must include disclosure of both financial and non-financial information about the issuer of the guaranteed security as well as any guarantors. Moreover, Securities Act registration causes both the issuer and the guarantors to become subject to Section 15(d)¹¹ of the Exchange Act. Section 15(d) requires all Securities Act registrants to file Exchange Act periodic reports for at least the fiscal year during which the related Securities Act registration statement became effective.

There are circumstances, however, where full Securities Act and Exchange Act disclosure by both the issuer and the guarantors may not be useful to an investment decision and, therefore, may not be necessary. For example, if a finance subsidiary issues debt securities guaranteed by its parent company, full disclosure of the finance subsidiary's financial information would be of little value. Instead, investors would look to the financial status of the parent company that guaranteed the debt to evaluate the likelihood of payment.

Subsidiary issuers and subsidiary guarantors raise a number of disclosure issues under the Securities Act and the Exchange Act. Included among these issues are:

- What information must issuers of guaranteed securities provide to potential investors in the registered offering;
- What information must guarantors provide to potential investors in the registered offering; and
- What information must those issuers and guarantors continue to provide to the secondary market.

In 1983, the staff addressed these issues in Staff Accounting Bulletin No. 53. In the 17 years since we published SAB 53, guaranteed securities have become significantly more complex. While the basic analysis of SAB 53 remains sound, the staff has had to expand on this analysis in response to registration statements and interpretive requests that involve new and complex transaction structures. In addition, the staff has responded to an increasing number of requests for relief from

Exchange Act reporting.¹² In 1999, approximately one-fourth of all interpretive, no-action, and exemptive requests acted on by the Division of Corporation Finance involved the application of SAB 53.¹³

The staff's interpretations, which balance the burden on issuers and guarantors to disclose required information fully with the investor's need for information, have addressed new and complex structures effectively. On March 5, 1999, we proposed rules and revisions to codify, in large part, the staff's current analysis regarding the obligations of the issuers and guarantors.¹⁴ We received 12 comment letters on our proposals.¹⁵

Today, we announce the adoption of those rules and revisions substantially as proposed. We believe these rules and revisions will:

- Eliminate uncertainty regarding financial statement requirements;
- Eliminate uncertainty regarding ongoing reporting;
- Eliminate the burden on issuers and guarantors to seek guidance regarding those requirements;¹⁶ and
- Simplify the staff's interpretive structure by applying one standard—condensed consolidating financial information—instead of the current approach that requires more or less financial disclosure based solely on the existence of non-guarantor subsidiaries.

We are revising Rule 3–10 of Regulation S–X to require, generally, the inclusion of condensed consolidating financial information as a condition to omitting the separate financial statements of a subsidiary issuer or subsidiary guarantor.¹⁷ There are,

¹² SAB 53 instructs issuers to file exemptive applications under Section 12(h) of the Exchange Act with regard to the Exchange Act reporting obligations of subsidiary issuers and subsidiary guarantors. Early in the development of SAB 53 issues, the staff began processing these exemptive requests as requests for no-action letters instead of exemptive applications. This process continues today. Throughout this release, we will refer to these requests as requests for no-action letters.

¹³ If requests for no-action letters under Exchange Act Rule 14a–8 [17 CFR 240.14a–8], the shareholder proposal rule, are excluded, nearly one-half of all Division of Corporation Finance no-action letters involved SAB 53.

¹⁴ Securities Act Release No. 7649 (March 5, 1999) [64 FR 10579].

¹⁵ These letters are available in File S7–7–99 in the Public Reference Room at 450 Fifth Street, N.W., Washington, D.C. 20549. Comment letters sent to the Commission electronically are available at our web site—www.sec.gov.

¹⁶ Issuers of guaranteed securities and guarantors could still request a no-action letter from the Division of Corporation Finance if today's amendments do not address their situation. The staff will apply the principles expressed in this release to those requests.

¹⁷ In connection with the revision to Rule 3–10, we are:

however, three situations in which no separate financial information or condensed consolidating financial information would be required, so long as the parent company financial statements include specified narrative disclosure. These situations arise

- Where the subsidiary issuer is a finance subsidiary and the parent company is the only guarantor of the securities;
- Where the parent company of the subsidiary issuer has no independent assets or operations,
- the parent company guarantees the securities,
- no subsidiary of the parent company guarantees the securities, and
- any subsidiaries of the parent company other than the issuer are minor; and
- Where the parent company issuer has no independent assets or operations, and
- all of the parent company's subsidiaries, other than minor subsidiaries, guarantee the securities.

We are adopting Exchange Act Rule 12h–5 to exempt from Exchange Act reporting requirements those subsidiary issuers and subsidiary guarantors that may omit separate financial statements under revised Rule 3–10. We are amending Form 20–F. We also are rescinding SAB 53.¹⁸

II. Financial Statement and Exchange Act Reporting Requirements for Subsidiary Guarantors and Subsidiary Issuers of Guaranteed Securities Before Today's Amendments

A. Financial Statement Requirements Before Today's Amendments

1. Basis for the Requirements

Rule 3–10 of Regulation S–X identifies which financial statements must be included in Securities Act registration statements, Exchange Act registration statements, and Exchange Act periodic reports for guarantors that are not filing under the small business issuer reporting system.¹⁹ Item 310 of

• Moving the financial statement requirement of affiliates whose securities collateralize registered securities from Rule 3–10 to new Rule 3–16; and

• Adopting new Notes 3 and 4 to Item 310 of Regulation S–B requiring small business issuers to present financial information for the fiscal periods they are required to present in accordance with amended Rule 3–10 and new Rule 3–16 of Regulation S–X.

¹⁸ Rule 3–10 and the positions expressed in this release will replace all prior Division of Corporation Finance no-action positions relating to SAB 53.

¹⁹ Before today's amendments, Rule 3–10 of Regulation S–X also prescribed financial statement requirements for affiliates of reporting issuers when the securities of such affiliates are the collateral for

¹⁰ 15 U.S.C. 77a et seq.

¹¹ 15 U.S.C. 78o(d).

Regulation S-B identifies those requirements for guarantors that are filing under the small business issuer reporting system.

Before today's amendments, those requirements were modified by SAB 53. In SAB 53, the staff responded to questions arising from the increased number of guaranteed securities offerings. SAB 53 did not amend Rule 3-10 of Regulation S-X. Instead, it described the approach the staff would take in its review of registration statements for two types of offerings of guaranteed debt securities:

- Securities issued by a subsidiary that are guaranteed by the parent company of that subsidiary; and
- Securities issued by a parent company that are guaranteed by a subsidiary of that company.

The staff has expanded the analysis of SAB 53 through its processing of registration statements and requests for no-action letters.

2. Financial Statement Requirements

SAB 53 and the expansion of its analysis have modified the financial statement requirements of Rule 3-10 and Item 310 for subsidiary guarantors of debt securities and subsidiary issuers of guaranteed debt securities. The basic assumption of the financial statement requirements before today's amendments was that there is no need for full financial statements of both the issuer of the guaranteed security and the guarantor when:

- The issuer or guarantor is a wholly-owned subsidiary of the parent company; and
- The guarantee is full and unconditional.

Under this analysis, if either of these conditions was not met, full financial statements for the subsidiary issuer or subsidiary guarantor would have to be included in the registration statement. If both conditions were met, the amount of financial information required for the subsidiary issuer or subsidiary guarantor would depend on whether the subsidiary had independent operations. For example,

- If the subsidiary issuer or subsidiary guarantor was a finance subsidiary, no separate financial statements were required; and
- If the subsidiary was not a finance subsidiary, there was a two-step process

for determining the appropriate financial information:

- If there was only one subsidiary issuer or subsidiary guarantor present, summarized financial information was appropriate; and
- In all other situations, condensed consolidating financial information was appropriate.

B. Exchange Act Reporting Requirements Before Today's Amendments

1. Basis for the Requirements

Exchange Act Section 15(d) requires separate periodic reports from both the issuer and the guarantor of securities offered under an effective Securities Act registration statement. SAB 53 only briefly addresses the Exchange Act reporting obligations of subsidiary issuers of parent company-guaranteed securities. In a footnote, SAB 53 states:

where the parent guarantor of an issuer subsidiary * * * is a reporting company under the Exchange Act, upon application to the Commission such a subsidiary would be conditionally exempted pursuant to Section 12(h)²⁰ of the Exchange Act from reporting obligations under such Act.

Since the issuance of SAB 53, the staff of the Division of Corporation Finance has responded to an increasing number of requests for no-action letters relating to Exchange Act reporting.

2. Exchange Act Reporting Requirements

The staff's analysis of no-action requests relating to Exchange Act periodic reporting is the same as its analysis of the financial statement requirements for subsidiary guarantors and subsidiary issuers of guaranteed securities in Securities Act registration statements. Therefore, if a subsidiary issuer or subsidiary guarantor was not required to include separate financial statements under the SAB 53 analysis, the staff would grant a request for a no-action letter relating to Exchange Act periodic reporting. Instead of separate reporting for the subsidiary issuer or subsidiary guarantor, the parent company would present in its periodic reports the same level of modified information regarding the subsidiary as it presented in the related Securities Act registration statement.

III. Today's Amendments to the Financial Statement and Exchange Act Reporting Requirements for Subsidiary Guarantors and Subsidiary Issuers of Guaranteed Securities

We believe that the requirements for subsidiary issuer and subsidiary

guarantor financial information should be provided in Regulation S-X. We also believe that the exemption from Exchange Act reporting should be provided in a rule that parallels the financial statement requirements. To accomplish this, we are adopting, in large part, the staff's current approach in these areas.

We believe today's amendments will provide investors with meaningful and comparable financial information about subsidiary issuers and subsidiary guarantors. We also believe that these amendments will provide significant benefits to subsidiary issuers and subsidiary guarantors by removing uncertainty about financial statement requirements and reducing the number of requests for no-action letters.

A. Rule 3-10 of Regulation S-X

We are adopting, as proposed, amendments to paragraph (a) of Rule 3-10. These amendments restate the general rule that all issuers or guarantors of registered securities must include separate financial statements.

We also are adopting new paragraphs (b) through (f) of Rule 3-10. These new paragraphs provide exceptions to the general rule of Rule 3-10(a) and permit modified financial information in registration statements and the parent company's periodic reports when

- A finance subsidiary issues securities that its parent company guarantees;
- An operating subsidiary issues securities that its parent company guarantees;
- A subsidiary issues securities that its parent company and one or more other subsidiaries of its parent company guarantee;
- A parent company issues securities that one of its subsidiaries guarantees; and
- A parent company issues securities that more than one of its subsidiaries guarantees.

Only one of these five paragraphs can apply to any particular offering and the subsequent Exchange Act reporting. With respect to these five paragraphs, the following two-part analysis determines whether modified financial information may be provided for subsidiary issuers and subsidiary guarantors.

- Is the subsidiary issuer or subsidiary guarantor 100% owned by its parent company?
- Are the guarantees full and unconditional?

If the answer to both questions is yes, modified financial information is allowed. If the answer to either question is no, modified financial information is

any class of the issuer's registered securities. Today's amendments move these requirements from Rule 3-10 to new Rule 3-16 of Regulation S-X. A more complete discussion of Rule 3-16 is located in Section III.D. "Financial statements of affiliates whose securities collateralize registered securities—Rule 3-16 of Regulation S-X."

²⁰ 15 U.S.C. 78l(h).

not allowed. We have adopted three other new paragraphs to Rule 3–10. Paragraph (g) provides the financial statement requirements for recently acquired subsidiary issuers and subsidiary guarantors. Paragraph (h) defines the following terms for purposes of Rule 3–10:

- 100% owned;
- Full and unconditional;
- Annual report;
- Quarterly report;
- No independent assets or operations;
- Minor;
- Finance subsidiary; and
- Operating subsidiary.

Paragraph (i) provides instructions for preparing the condensed consolidating financial information required by paragraphs (c) through (f) of Rule 3–10.

1. Two-Part Analysis To Determine Whether Modified Financial Information May Be Provided

a. The Meaning of “100% Owned”

Under SAB 53, a subsidiary was “wholly owned” if all of its outstanding voting shares and any outstanding securities convertible into its voting shares were owned, either directly or indirectly, by its parent company.²¹ This meaning differs from the general definition of “wholly-owned subsidiary” in Rule 1–02(aa) of Regulation S–X.²² Rule 1–02(aa) treats a subsidiary as wholly owned if substantially all of its voting shares are held by its parent company. We proposed that the meaning of “wholly owned” for the purposes of Rule 3–10 would be, in large part, the same as the staff’s analysis under SAB 53.

The comments on the proposed definition of wholly owned in Rule 3–10 varied significantly. One commenter suggested that the special relief granted by SAB 53 should be extended to any issuer or guarantor that is a subsidiary.²³ Another commenter believed just the opposite, indicating its support for the definition as proposed.²⁴ A third commenter suggested that reduced financial reporting should be permitted for 100%-owned subsidiaries and subsidiaries whose minority shareholders consist solely of affiliates of the consolidated group.²⁵

We are adopting the meaning of “wholly owned” that was used under

SAB 53. However, we have used the term “100% owned” in Rule 3–10 to avoid confusion with the definition of “wholly-owned subsidiary” in Rule 1–02(aa) of Regulation S–X. We discuss the definition of 100% owned and the reasons for adopting that definition in the following sections.²⁶

i. Subsidiaries in Corporate Form

(A) Definition of 100% Owned

A subsidiary in corporate form is 100% owned for the purposes of Rule 3–10 if all of its outstanding voting shares and any outstanding securities convertible into its voting shares are owned, directly or indirectly, by its parent company.²⁷ We are adopting this definition because it assures investors in the guaranteed securities that there is no competing common equity interest in the assets or revenues of the subsidiary. This allows investors to evaluate the creditworthiness of the parent and subsidiary as a single, indivisible business. If a third party holds an interest in the subsidiary, the risks associated with investment in parent and subsidiary are not identical. Where those risks are not identical, there is not the financial unity between the subsidiary and its parent that is needed to justify the modified financial information permitted by paragraphs (b) through (f) of Rule 3–10.

To remain 100% owned, a subsidiary corporation may not issue any securities convertible into its voting shares unless those convertible securities are owned, directly or indirectly, by its parent company. This would preclude the use of options that are exercisable into voting shares unless those options are owned, directly or indirectly, by the subsidiary’s parent company.

One commenter addressed convertible securities.²⁸ That commenter believed that a subsidiary that has issued securities convertible into its voting

securities to someone other than its parent company should be considered 100% owned if the parent company has the unilateral right to reacquire such instruments for a fixed or determinable price before their conversion. We do not agree that the definition of 100% owned should include a subsidiary that issued to a third party securities convertible into its voting shares, irrespective of the parent’s right to repurchase. A subsidiary that has issued to any person other than its parent company securities that are convertible into its voting stock does not have the financial unity with its parent company that is necessary to qualify for the modified financial information permitted by paragraphs (b) through (f) of Rule 3–10.

(B) Interpretive Position Regarding Foreign Issuers and Guarantors

The definition of 100% owned in Rule 3–10 precludes any outside ownership of voting shares for subsidiary corporations. Therefore, subsidiaries organized in a jurisdiction that requires directors to own shares would not meet the 100%-owned test. Nonetheless, we concur in the staff’s response to Crown Cork & Seal Company, Inc. (March 10, 1997), in which the staff agreed to a no-action request under SAB 53 from a subsidiary organized in the Republic of France even though it had more than one voting shareholder. That no-action request stated that French law required the subsidiary to have a total of seven shareholders and also required each director to own at least one share. The request explained that, in order to comply with this requirement, the parent company would transfer approximately six shares, equaling approximately 0.24% of the parent company’s outstanding shares, to its directors. In granting the no-action position, the staff noted that the non-parent company ownership was at the minimum level required to comply with French law. We have not included this exception in amended Rule 3–10 because it is an uncommon situation that should be handled through the no-action request process. However, the staff will continue to recognize the exception presented by Crown Cork & Seal Company, Inc., as well as any future no-action requests from other issuers under substantially similar facts.²⁹

²⁶ We also have included Appendix A at the end of this release to further illustrate the meaning of 100% owned. We included four appendices in the proposing release to give guidance on the application of the proposed rules. We are rescinding those appendices. Issuers and guarantors should not rely on those appendices. Instead, issuers and guarantors should consider the appendices to this adopting release when applying today’s amendments to specific situations. The staff intends to publish additional guidance on the application of today’s amendments.

²⁷ Rule 1–02(z) of Regulation S–X [17 CFR 210.1–02(z)] defines “voting shares.” All securities of a subsidiary that confer the right to elect directors or their functional equivalents annually, whether or not those securities are equity or debt, must be held by the parent to satisfy the 100%-owned test. This test is unaffected by the existence of other securities that grant the right to vote in the event of special circumstances, such as a default.

²⁸ Comment letter of PricewaterhouseCoopers (May 4, 1999).

²⁹ If any issuer and guarantor fail to meet the 100%-owned definition, but can demonstrate that their situation provides them with the financial unity needed to qualify for the modified financial information permitted by paragraphs (b) through (f) of Rule 3–10, they may request relief from the

²¹ See, e.g., Citizens Utilities Company (May 20, 1996).

²² 17 CFR 210.1–02(aa).

²³ Comment letter of Sullivan & Cromwell (May 4, 1999).

²⁴ Comment letter of PricewaterhouseCoopers (May 4, 1999).

²⁵ Comment letter of KPMG LLP (May 4, 1999).

ii. Subsidiaries in Other Than Corporate Form

We also proposed a separate definition of 100% owned for subsidiaries that are not in corporate form. As proposed, a non-corporate entity would be 100% owned if its parent company owned all of its outstanding interests. We have altered this definition slightly. As adopted, a subsidiary not in corporate form is 100% owned if all outstanding interests in that subsidiary are owned, either directly or indirectly, by its parent company other than:

- Securities to which Rule 3–10 applies that are guaranteed by its parent company and, if applicable, other 100%-owned subsidiaries of its parent company; and
- Guarantees of securities issued by its parent company and, if applicable, other 100%-owned subsidiaries of its parent company.

This revision recognizes that the securities issued in the transaction that makes the subsidiary subject to Rule 3–10 may be “interests” for purposes of the definition of 100% owned.

One commenter suggested that the definition of 100% owned for an unincorporated entity should be changed so that relief would be available so long as the parent owns all or substantially all of the “participating” ownership interests in the entity.³⁰ We are not adopting this suggestion. Unincorporated entities operate differently than corporations and one form of participation in the operation of an entity may be separate from another form of participation in the entity. For example, in a limited liability corporation, the ability to vote can be separated from the ability to manage the financial affairs of the entity. The staff historically has allowed, and Rule 3–10 will allow, modified financial information only when the parent and subsidiary or subsidiaries have financial unity.

b. The Meaning of “Full and Unconditional”

We proposed to define a “full and unconditional” guarantee consistent with the staff’s interpretation of that term for purposes of SAB 53. We are adopting the definition as proposed.

The definition we adopt today is intended to limit the availability of the

modified financial information permitted by paragraphs (b) through (f) of Rule 3–10 to those situations where the payment obligations of the issuer and guarantor are essentially identical. Under Rule 3–10, a guarantee is full and unconditional if

when an issuer of a guaranteed security has failed to make a scheduled payment, the guarantor is obligated to make the scheduled payment immediately and, if it doesn’t, any holder of the guaranteed security may immediately bring suit directly against the guarantor for payment of all amounts due and payable.³¹

Under this definition, a guarantee is not full and unconditional if the amount of the guarantor’s liability is less than the issuer’s or, should the issuer default, the guarantor’s payment schedule differs from the issuer’s payment schedule. There can be no conditions, beyond the issuer’s failure to pay, to the guarantor’s payment obligation. For example, the holder cannot be required to exhaust its remedies against the issuer before seeking payment from the guarantor.

In the following three sections, we discuss specific interpretive issues presented by the definition of full and unconditional guarantee.

i. A Guarantee Is Not Full and Unconditional When It Is Not Operative Until Some Time After Default

One commenter noted that, under the proposed definition, a guarantee that became due only after the passage of some time period after default would not be full and unconditional under Rule 3–10.³² This commenter indicated that this definition would not comport with a debt structure used in some European transactions, where there is a “standstill” period before the guarantee can be enforced. The commenter expressed the view that the “standstill” requirement should not result in additional disclosure obligations and the proposed definition would, likely, be detrimental to investors in European debt securities. We have not revised the definition as suggested. The presence of a delay before the guarantee could be enforced would undermine the financial unity that is necessary for the modified financial information permitted by paragraphs (b) through (f) of Rule 3–10. Specifically, if there is any period of time during which the investor may not proceed against the guarantor(s), then it is necessary for that investor to be able to fully evaluate the issuer and guarantor(s) separately. Because the payment obligation does not fall

uniformly across the issuer and the related guarantors when there is a delay before the guarantee can be enforced, each party in that structure must provide separate financial statements.

ii. A Guarantee Can Be Full and Unconditional Even If It Has a Fraudulent Conveyance “Savings Clause”

A guarantee can be full and unconditional even if it includes a “savings clause” related to bankruptcy and fraudulent conveyance laws. These savings clauses prevent the guarantor from making an otherwise required payment if the money needed to make that payment is first recoverable by other creditors under bankruptcy or fraudulent conveyance laws. However, if any clause places a specific limit on the amount of the guarantor’s regular payment obligation to avoid application of bankruptcy or fraudulent conveyance laws, that guarantee would not be full and unconditional.

For example, the following savings clauses would not defeat the full and unconditional nature of the guarantee.

- The guarantor’s obligation under the guarantee is limited to “the maximum amount that can be guaranteed without constituting a fraudulent conveyance or fraudulent transfer under applicable insolvency laws.”
- The guarantee is enforceable “to the fullest extent permitted by law.”
- The following savings clauses would defeat the full and unconditional nature of the guarantee.
 - The guarantee is enforceable “up to \$XX.”
 - The guarantor guarantees the indebtedness “up to \$XX.”
 - The guarantee is “limited to \$XX in order to prevent the guarantor from violating applicable fraudulent conveyance or transfer laws.”
 - The guarantee is enforceable “up to XX% of the guarantor’s current assets.”
 - The guarantee is “limited to XX% of the guarantor’s current assets in order to prevent the guarantor from violating applicable fraudulent conveyance or transfer laws.”
 - The guarantee is enforceable “so long as it would not result in the guarantor having less than \$XX in net assets [or other financial measure].”

iii. A Guarantee Can Be Full and Unconditional Even if it Has Different Subordination Terms Than the Guaranteed Securities

A guarantee can be full and unconditional despite different subordination terms between the

Division of Corporation Finance. In its consideration of these requests, the staff will consider the principles set forth in this release regarding the significance of the 100%-owned definition.

³⁰ Comment letter of Sullivan & Cromwell (May 4, 1999).

³¹ See Rule 3–10(h)(2).

³² Comment letters of Latham & Watkins (July 15, 1999, and July 6, 2000).

guaranteed security and the guarantee.³³ For example, a parent company's guarantee can be full and unconditional even if the subsidiary's debt obligation ranks senior to all other debt of that subsidiary and the parent company's guarantee ranks junior to other debt obligations of the parent company. Although different subordination terms mean security holders have different rights in the priority of payment with respect to the issuer and the guarantor, both the issuer and the guarantor remain fully liable to holders for all amounts due under the guaranteed security.

One commenter agreed that subordination terms among the guaranteed security and the guarantees should not affect the full and unconditional analysis.³⁴ However, that commenter felt that condensed consolidating financial information should be expanded in these cases to require separate columns grouping the guarantors by priority position or subordination. We are not expanding the condensed consolidating requirements as suggested because we believe that the condensed consolidating financial information provides the appropriate level of information to investors.

2. Rule 3-10(b) Through (f)

a. Preliminary Conditions to the Availability of Rule 3-10(b) Through (f)

If either the guarantee is not full and unconditional or the subsidiary is not 100% owned by its parent company, then modified financial information would not be allowed. Our discussion of amended Rule 3-10 in subsections b. through f., below, assumes that each of these conditions has been met.

b. Finance Subsidiary Issuer of Securities Guaranteed by its Parent Company Only

We proposed to amend Rule 3-10 to codify SAB 53's treatment of finance subsidiary issuers of securities that are guaranteed by the parent company. As adopted, paragraph (b) of Rule 3-10 provides that subsidiary issuers would not be required to include any financial information if:

- The subsidiary is a finance subsidiary;³⁵

- The parent company of the subsidiary issuer guarantees the securities;
- No other subsidiary of the parent company guarantees the securities;
- The parent company's financial statements are filed for the periods specified by Rules 3-01 and 3-02 of Regulation S-X;³⁶ and
- The parent company's financial statements include a footnote stating that the issuer is a 100%-owned finance subsidiary of the parent company and the parent company has fully and unconditionally guaranteed the securities.

In response to comments, we have added a note to paragraph (b) stating that if a subsidiary issuer satisfies the requirements of this paragraph but for the fact that it co-issued the securities, jointly and severally, with its parent company, the parent company may present its financial information with respect to the subsidiary as paragraph (b) permits.

One commenter asked us to clarify what happens when a finance subsidiary ceases to meet the definition of finance subsidiary.³⁷ At that time, the subsidiary should be treated as an operating subsidiary. The parent company is not required to amend any reports for periods before the subsidiary stopped being a finance subsidiary. The parent company must present condensed consolidating financial information for the subsidiary when the subsidiary ceases to be a finance subsidiary. That is, the parent company must present condensed consolidating financial information for the operating subsidiary in the Exchange Act report for the period in which the subsidiary stopped being a finance subsidiary.

In an offering of securities that is registered under the shelf registration system,³⁸ if the finance subsidiary ceases to meet the definition of finance subsidiary, the registration statement must be amended to include the appropriate financial information before any further offers may be made. Ordinarily, under the shelf registration system, this information would have to be included in the registration statement through a post-effective amendment. However, offerings that are registered on Form S-3³⁹ could satisfy this requirement by filing the financial

information on a Form 8-K⁴⁰ that is incorporated by reference.⁴¹

c. Operating Subsidiary Issuer of Securities Guaranteed by its Parent Company Only

We proposed to amend Rule 3-10 to address specifically the structure where the parent company guarantees the securities issued by a subsidiary that is not a finance subsidiary. SAB 53 permitted the parent company's financial statement footnotes to include summarized financial information regarding the operating subsidiary issuer. Consistent with our view that condensed consolidating financial information is more appropriate, we are adopting paragraph (c) of Rule 3-10 to provide that these issuers need not include separate financial statements if:

- The parent company guarantees the securities;
- No subsidiary of the parent company guarantees the securities;
- The parent company's financial statements are filed for the periods specified by Rules 3-01 and 3-02 of Regulation S-X; and
- the parent company's financial statement footnotes include condensed consolidating financial information for the same periods with a separate column for:
 - The parent company;
 - The subsidiary issuer;
 - Any other subsidiaries of the parent on a combined basis;
 - Consolidating adjustments; and
 - The total consolidated amounts.

We are adopting the paragraph as proposed with the addition of three notes. First, we have added a note stating that the condensed consolidating financial information may be omitted if:

- The parent company has no independent assets or operations;⁴²
- Any subsidiaries other than the subsidiary issuer are minor;⁴³ and

⁴⁰ 17 CFR 249.308.

⁴¹ Similarly, offerings that are registered on Form F-3 [17 CFR 239.33] could satisfy this requirement by filing the financial information on a Form 6-K [17 CFR 249.306] that is incorporated by reference.

⁴² Rule 3-10(h)(5) states that, for purposes of Rule 3-10, a parent company has no independent assets or operations if "its total assets, revenues, income from continuing operations before income taxes, and cash flows from operating activities (excluding amounts related to its investment in its consolidated subsidiaries) are each less than 3% of the corresponding consolidated amounts."

⁴³ Rule 3-10(h)(6) states that, for purposes of Rule 3-10, "a subsidiary is *minor* if its total assets, stockholders' equity, revenues, income from continuing operations before income taxes, and cash flows from operating activities are each less than 3% of the parent company's corresponding consolidated amounts." A note to this definition indicates that when considering a group of subsidiaries, the definition applies to each

³³ See Williams Scotsman, Inc. (March 19, 1998).

³⁴ Comment letter of PricewaterhouseCoopers (May 4, 1999).

³⁵ Rule 3-10(h)(7) states that a subsidiary is a finance subsidiary if "it has no assets, operations, revenues or cash flows other than those related to the issuance, administration and repayment of the security being registered and any other securities guaranteed by its parent company."

³⁶ 17 CFR 210.3-01 and 17 CFR 210.3-02. Rule 3-10(a)(3) states that foreign parent companies should look to Item 8.A of Form 20-F to determine the periods for which financial statements are required.

³⁷ Comment letter of Arthur Andersen (May 4, 1999).

³⁸ See Securities Act Rule 415 [17 CFR 230.415].

³⁹ 17 CFR 239.13.

• The parent company's financial statements include a footnote stating that the parent company has no independent assets or operations, the guarantee is full and unconditional and any subsidiaries other than the subsidiary issuer are minor.

This note was added to the proposed rule based on comments we received suggesting that when the parent company is a holding company and the subsidiary issuer is the only subsidiary other than minor subsidiaries, the subsidiary issuer should be treated like a finance subsidiary. We agree that under these circumstances the consolidated financial statements, when combined with the required narrative information, provide substantially the same information as condensed consolidating financial information. Thus, the condensed consolidating financial information need not be presented.

Second, we have added a note stating that the separate column for other subsidiaries is not required when the parent company has independent assets or operations, but the other subsidiaries are minor.

Third, we have added a note stating that if a subsidiary issuer satisfies the requirements of this paragraph but for the fact that it co-issued the securities, jointly and severally, with its parent company, the parent company may present its financial information with respect to the subsidiary as paragraph (c) permits.

d. Subsidiary Issuer of Securities Guaranteed By its Parent Company and One or More Other Subsidiaries of That Parent Company

We proposed to codify the staff's position regarding the structure where a subsidiary issues securities and both its parent company and one or more other subsidiaries of that parent company are guarantors. As adopted, paragraph (d) of Rule 3-10 provides that these subsidiary issuers and subsidiary guarantors need not include separate financial statements if:

- The guarantees are joint and several;
- The parent company's financial statements are filed for the periods specified by Rules 3-01 and 3-02 of Regulation S-X; and
- The parent company's financial statement footnotes include condensed consolidating financial information for the same periods with a separate column for
 - The parent company;

- the subsidiary issuer;
- the guarantor subsidiaries on a combined basis;
- any other subsidiaries on a combined basis;
- consolidating adjustments; and
- the total consolidated amounts.

This paragraph applies in the same manner regardless of whether the issuer is a finance subsidiary or an operating subsidiary.

We are adopting this paragraph as proposed with the addition of four notes. First, we added a note stating that the separate column for other subsidiaries is not required when those other subsidiaries are minor.

Second, we added a note stating that if a subsidiary issuer satisfies the requirements of this paragraph but for the fact that it co-issued the securities, jointly and severally, with its parent company, the parent company may present its financial information with respect to the subsidiaries as paragraph (d) permits.

Third, we added a note addressing guarantees that are not joint and several. That note states that

- if
 - there is one subsidiary guarantor and that subsidiary's guarantee is not joint and several with the parent company's guarantee, or
 - there is more than one subsidiary guarantor and any of the subsidiary guarantees is not joint and several with the guarantees of the parent company and the other subsidiaries,
- Then
 - each subsidiary guarantor whose guarantee is not joint and several need not include separate financial statements, but
 - the condensed consolidating financial information must include a separate column for each subsidiary guarantor whose guarantee is not joint and several.

Fourth, we added a note addressing the situation when the parent company has no independent assets or operations, the subsidiary issuer is a finance company, and all of the parent company's other subsidiaries guarantee the securities on a full and unconditional and joint and several basis. In that situation, the consolidated financial statements, when combined with the required narrative information, provide substantially the same information as condensed consolidating financial information. Thus, the condensed consolidating financial information need not be presented.

e. Single Subsidiary Guarantor of Securities Issued By Its Parent Company

We proposed to codify the staff's positions regarding the structure where a parent company issues securities and one of its subsidiaries guarantees those securities. As adopted, paragraph (e) of Rule 3-10 provides that the subsidiary guarantor need not include separate financial statements if:

- No other subsidiary of that parent company guarantees the securities;
- The parent company's financial statements are filed for the periods specified by Rules 3-01 and 3-02 of Regulation S-X; and
- The parent company's financial statement footnotes include condensed consolidating financial information for the same periods with a separate column for
 - the parent company;
 - the subsidiary guarantor;
 - any other subsidiaries of the parent on a combined basis;
 - consolidating adjustments; and
 - the total consolidated amounts.

This paragraph applies in the same manner regardless of whether the subsidiary guarantor is a finance subsidiary or an operating subsidiary.

We are adopting this paragraph as proposed with the addition of three notes. First we have added a note stating that the condensed consolidating financial information may be omitted if:

- The parent company has no independent assets or operations;
- Any subsidiaries other than the guarantor are minor; and
- The parent company's financial statements include a footnote stating that the parent company has no independent assets or operations, the guarantee is full and unconditional and any non-guarantor subsidiaries are minor.

Second, we added a note stating that the separate column for other subsidiaries is not required when the parent company has independent assets or operations, but the other subsidiaries are minor.

Third, we added a note stating that this paragraph does not apply if the subsidiary co-issued the securities, jointly and severally, with its parent company. Instead,

- If the subsidiary is a finance subsidiary, paragraph (b) would apply; and
- If the subsidiary is an operating subsidiary, paragraph (c) would apply.

We added this note to eliminate any potential confusion regarding which paragraph applies in co-issuer situations.

subsidary in that group individually and to all subsidiaries in that group in the aggregate.

f. Multiple Subsidiary Guarantors of Securities Issued By Their Parent Company

We proposed to codify the staff's position for the structure when a parent company issues securities and more than one of its subsidiaries guarantees the securities. As adopted, paragraph (f) of Rule 3-10 provides that the subsidiary guarantors need not include separate financial statements if:

- The guarantees are joint and several;
- The parent company's financial statements are filed for the periods specified by Rules 3-01 and 3-02 of Regulation S-X; and
- The parent company's financial statement footnotes include condensed consolidating financial information for the same periods with a separate column for
 - the parent company;
 - the subsidiary guarantors on a combined basis;
 - any other subsidiaries on a combined basis;
 - consolidating adjustments; and
 - the total consolidated amounts.

We are adopting this paragraph as proposed, with the addition of three notes. First, we have added a note stating that the condensed consolidating financial information may be omitted if:

- The parent company has no independent assets or operations;
- Any subsidiaries other than the subsidiary guarantors are minor; and
- The parent company's financial statements include a footnote stating that the parent company has no independent assets or operations, the guarantees are full and unconditional and joint and several, and any non-guarantor subsidiaries are minor.

Second, we added a note stating that the separate column for other subsidiaries is not required when the parent company has independent assets or operations, but the other subsidiaries are minor.

Third, we added a note addressing guarantees that are not joint and several. That note states that

- If
 - any of the subsidiary guarantees is not joint and several with the guarantees of the other subsidiaries,
 - Then
 - each subsidiary guarantor whose guarantee is not joint and several need not include separate financial statements, but
 - the condensed consolidating financial information must include a separate column for each subsidiary guarantor whose guarantee is not joint and several.

3. Condensed Consolidating Financial Information Required By Rule 3-10(c) Through (f)

Under today's amendments to Rule 3-10, a subsidiary may rely on one of the exceptions in paragraphs (c) through (f) if it is otherwise eligible for that exception and the parent company's financial statements include a footnote presenting condensed consolidating financial information.

a. Reasons for Requiring Condensed Consolidating Financial Information Instead of Summarized Financial Information

Under SAB 53, subsidiary issuers were permitted to include summarized financial information as described in Rule 1-02(bb) of Regulation S-X.⁴⁴ Summarized financial information originally was intended only to inform investors about a registrant's equity investments in unconsolidated affiliates. The summarized financial information shows the general, indirect effect of the subsidiaries on their parent company's financial condition. This type of financial information is appropriate when the investment decision is based solely on the financial condition of the parent company.

However, in SAB 53, the staff did not contemplate the widespread use of summarized financial information as the primary financial information for assessing the creditworthiness of a subsidiary guarantor. The staff also did not contemplate more complex guarantee structures where investors must assess the subsidiary's financial condition more completely and independently of its parent company and other subsidiaries of its parent company. Summarized financial information is inadequate for this purpose. For example, although cash flow information is significant in assessing creditworthiness, summarized financial information includes no cash flow information.

Further, summarized financial information, as the staff recognized in its application of SAB 53, raised the question of how to deal with multiple guarantors. Many structures presented to the staff involved a subsidiary issuer, a parent company guarantor, multiple subsidiary guarantors, and multiple subsidiaries that are not guarantors. Other structures involved more than 100 subsidiary guarantors. A strict application of SAB 53 in that situation would have required more than 100 sets of summarized financial information.

⁴⁴ The staff expanded this relief to subsidiary guarantors in Anheuser-Busch Companies, Inc. (April 2, 1987).

Not only would that disclosure have been burdensome for the registrant to provide, it is unlikely to have been useful to investors.

Through interpretive requests and the review and comment process, the staff began to rely on the inclusion of condensed consolidating financial information in lieu of summarized financial information in most situations.⁴⁵ Condensed consolidating financial information requires the columnar presentation of each category of parent and subsidiary as issuer, guarantor, or non-guarantor.⁴⁶

In today's amendments to Rule 3-10, we are requiring condensed consolidating financial information as a condition to omitting separate financial statements. We are requiring condensed consolidating financial information because it clearly distinguishes the assets, liabilities, revenues, expenses, and cash flows of the entities that are legally obligated under the indenture from those that are not.⁴⁷ Furthermore, condensed consolidating financial information provides the same level of detail about the financial position, results of operations, and cash flows of subsidiary issuers and subsidiary guarantors that investors are accustomed to obtaining in interim financial statements of a registrant. It also facilitates analysis of trends affecting subsidiary issuers and subsidiary guarantors and relationships among the various components of a consolidated organization.

b. Comments Regarding Condensed Consolidating Financial Information

We requested comment on whether condensed consolidating financial information was the proper level of disclosure. The commenters generally expressed support for the proposed

⁴⁵ The staff required condensed consolidating financial information in all situations except those specifically addressed in SAB 53—specifically, those where (a) there was a single subsidiary issuer or, where there was a parent issuer and a subsidiary guarantee, that guarantee was provided by either a single subsidiary or all subsidiaries; or (b) the issuer was a finance subsidiary and the parent was the sole guarantor. The staff first accepted condensed consolidating financial information in connection with its case-by-case review of Securities Act registration statements. Consistent with the earlier development of SAB 53 interpretation, the staff applied the same analysis to no-action requests relating to Exchange Act reporting. *See, e.g.*, Chicago & North Western Acquisition Corp. (February 6, 1990); EPIC Properties, Inc. (March 13, 1992).

⁴⁶ The staff permits subsidiary guarantors to combine financial information in one column if their guarantees are joint and several.

⁴⁷ Summarized financial information may obscure these distinctions, particularly if subsidiary guarantors themselves have consolidated operating subsidiaries that are not guarantors.

requirement for condensed consolidating financial information. One commenter suggested an alternative to condensed consolidating financial information where summarized financial information would have been permitted before today's amendments.⁴⁸ That commenter suggested that we expand the summarized financial information specified by Rule 1-02(bb) to include additional line items and cash flow information.

Another commenter expressed the view that condensed consolidating financial information results in a presentation that is inconsistent with other financial statement requirements of Regulation S-X because it requires parent companies to present investments in all subsidiaries, and subsidiary issuer and subsidiary guarantor columns to present investments in non-guarantor subsidiaries, on an unconsolidated basis.⁴⁹ That commenter believed that the distinction between a 100%-owned subsidiary issuer or subsidiary guarantor and a 100%-owned non-guarantor subsidiary should not affect an investor's assessment of the parent company's ability to satisfy the debt obligations. The commenter also believed that condensed consolidating financial information is unduly burdensome to prepare and does not fully depict the "structural subordination" of an issuer's registered classes of guaranteed debt to other obligations of non-guarantor subsidiaries in many debt structures. Accordingly, the commenter proposed that the summarized financial information approach, expanded to include cash flow information, be adopted for all issuers and guarantors who exhibit evidence of the ability to satisfy their obligations and are in good financial condition. This suggestion would require a merit determination each time financial information is presented.

For the reasons discussed above, we are adopting the condensed consolidating financial information requirement as proposed. We continue to believe that condensed consolidating financial information provides the most meaningful presentation to permit investors to evaluate the ability to pay of those entities that are legally obligated under the debt and the guarantee(s). We also believe the approach is more adaptable to new and complex debt instruments and structures.

In our view, summarized financial information, even if modified to include additional data, provides less complete information about subsidiary issuers and subsidiary guarantors and is less flexible than condensed consolidating financial information. It also would be difficult to develop and administer a meaningful and practical difference in presentation requirements based on the financial condition of the subsidiary or parent company across the wide range of debt instruments, issuers and industries. Further, it seems that the likely result of the summarized financial information approach in complex structures would be the inclusion of multiple sets of summarized financial information. The relationship of the summarized data to the consolidated financial statements of the parent would likely be unclear, and the assets and operations of particular subsidiary issuers or subsidiary guarantors would likely be duplicated by inclusion in multiple sets of data. In large part, these same factors led the staff to develop the condensed consolidating financial information approach a number of years ago.

4. Securities to Which Rule 3-10 Applies

a. Rule 3-10(a) Requires Separate Financial Statements for Each Issuer of Registered Guaranteed Securities and Each Guarantor of Registered Securities

Rule 3-10(a) requires, as a general rule, separate financial statements for "every issuer of a registered security that is guaranteed and every guarantor of a registered security."⁵⁰ This requirement applies regardless of:

- The relationship between the issuer and the guarantor(s);

⁵⁰ One commenter asked us to clarify the application of Rule 3-10 when the guarantee does not run to the benefit of the debt holders and, thus, would not be a "security" itself. See Comment letter of PricewaterhouseCoopers (May 4, 1999). That commenter also asked that the rule be expanded to cover situations in which the staff historically has asked for financial disclosures by guarantors or credit enhancers even when the guarantee that is not a security or the credit enhancement does not run directly to the holders of the related security.

Typically, in those situations, the issuer of the guarantee or provider of the credit enhancement does not incur a Rule 3-10(a) financial statement obligation or a Section 15(d) reporting obligation as a result of the guarantee or the credit enhancement. Nevertheless, when a party provides such a guarantee or credit enhancement, its financial information often is material to investors in the related security. If that information is material, the staff may ask that the guarantor or credit enhancer's financial statements be disclosed. These situations are beyond the scope of today's initiative. We have not amended Rule 3-10 in response to this comment and today's amendments do not affect the staff's practices with regard to these types of guarantees and credit enhancements.

- The nature of the guaranteed security; or
- Whether the guarantee is full and unconditional.

b. Guaranteed Securities for Which Paragraphs (b) Through (f) of Rule 3-10 May Provide an Exception to the Requirement of Rule 3-10(a)

We have adopted five exceptions to the general rule of Rule 3-10(a) in recognition that there are specific types of securities, guarantees, and related parties for which modified financial information is appropriate. We are providing, as proposed, that the modified financial information permitted by paragraphs (b) through (f) be available only for guaranteed debt and guaranteed preferred securities that have payment terms that are substantially the same as debt.⁵¹ Under this standard, the payment terms of the preferred securities must mandate redemption and/or dividend payments.⁵²

i. The Modified Financial Information Permitted by Paragraphs (b) Through (f) is Available Only for Guaranteed Debt and Debt-Like Securities

The modified financial information permitted by paragraphs (b) through (f) will be available only for guaranteed debt and debt-like instruments. Neither the form of the security nor its title will determine the availability of those paragraphs. Instead, the substance of the obligation created by the security will be determinative. The characteristics that identify a guaranteed security as debt or debt-like for this purpose are:

- The issuer has a contractual obligation to pay a fixed sum at a fixed time; and
- Where the obligation to make such payments is cumulative, a set amount of interest must be paid.

The fact that disbursements on the security may be called "payments," "distributions," or "dividends" rather than "interest" or that holders are entitled to "liquidation" or "mandatory redemption" rather than "principal" payments does not defeat their status as debt or debt-like for this purpose. Similarly, the fact that a security is called "preferred stock" or "debt" does not bring it within the rule if the

⁵¹ These securities include trust preferred securities. We discuss these securities later in this section.

⁵² Preferred securities normally carry very limited voting rights, such as the right of holders to vote on matters affecting their rights as shareholders or business combinations. The right to elect directors is normally conferred only when the issuer has failed to declare or pay a dividend required by the security.

⁴⁸ Comment letter of KPMG LLP (May 4, 1999).

⁴⁹ Comment letters of Time Warner, Inc. (July 8, 1999 and August 10, 1999).

security does not bear the necessary characteristics of debt.

The phrase "set amount of interest" is not intended to mean "fixed amount of interest." The modified financial information permitted by paragraphs (b) through (f) is available for floating and adjustable rate securities, as well as indexed securities, as long as the payment obligation is set in the debt instrument and can be determined from objective indices or other factors that are outside the discretion of the obligor.

In the following sections, we discuss two issues that arise because paragraphs (b) through (f) of Rule 3-10 are available for debt-like securities. Specifically, we discuss:

- When a guarantee of preferred securities is full and unconditional for purposes of Rule 3-10; and
- The application of Rule 3-10 to "trust preferred securities."

(A) Full and Unconditional Guarantee of Preferred Securities

For the modified financial information permitted by paragraphs (b) through (f) of Rule 3-10 to be available for guaranteed preferred securities, the guarantor must fully and unconditionally guarantee all of the issuer's payment obligations under the certificate of designations or other instrument that governs the preferred securities. The guarantor must guarantee the payment, when due, of:

- All accumulated and unpaid dividends that have been declared on the preferred securities out of funds legally available for the payment of dividends;
- The redemption price, on redemption of the preferred securities, including all accumulated and unpaid dividends; and
- Upon liquidation of the issuer of the preferred securities, the aggregate stated liquidation preference and all accumulated and unpaid dividends, whether or not declared, without regard to whether the issuer has sufficient assets to make full payment as required on liquidation.

Some guarantees of preferred securities limit the guarantor's redemption and liquidation payments to the amount of funds or assets that are legally available to the issuer of the preferred securities. These guarantees would not be full and unconditional. For example, guarantees that contain the following provisions would not be full and unconditional.

- The guarantor guarantees, on redemption of the preferred securities, the redemption price, including all accumulated and unpaid dividends,

from funds legally available therefor to the issuer.

• Upon liquidation of the issuer of the preferred securities, the guarantor agrees to pay the lesser of:

- The aggregate stated liquidation preference and all accumulated and unpaid dividends, whether or not declared; and
- The amount of assets of the issuer of the preferred securities legally available for distribution to holders of the preferred stock in liquidation.

(B) Trust Preferred Securities

Trust preferred securities generally are issued by a special purpose business trust created by its parent company.⁵³ The trust exists only to issue the preferred securities and hold debt securities issued by its parent company.⁵⁴ Payment obligations of the trust are ensured not by a single agreement called a guarantee, but through several agreements and by the terms of the debt securities that the trust holds. The agreements normally include a guarantee and an expense undertaking from the parent company, the trust indenture for the debt securities the trust holds, and the trust declaration of the trust itself. In applying SAB 53 to these securities, the staff agreed with the view that the bundle of rights provided by these agreements and the debt securities held by the trust, usually called the "back-up undertakings," is the equivalent of a "full and unconditional" guarantee of the trust's payment obligations.

Based on the same reasoning as the staff has applied to these securities, we believe that the modified financial information permitted by paragraphs (b) through (f) of Rule 3-10 should be available for these securities where:

- Holders are entitled to receive periodic payments that are cumulative if unpaid and holders are entitled to receive a fixed liquidation amount;⁵⁵ and
- The "back-up undertakings" place the investor in the same position as if the parent company had fully and unconditionally guaranteed the trust's

⁵³ Other names for these securities include "monthly income preferred securities" or "quarterly income preferred securities." These securities generally are sold under proprietary names such as MIPs, QUIPs, or TOPRs.

⁵⁴ While these securities typically are issued by a business trust, they also may be issued by a limited partnership or a limited liability corporation.

⁵⁵ As with other debt-like securities, the modified financial information permitted by paragraphs (b) through (f) would be available only where the failure to make the periodic payment would have the same result as a default on a required payment of interest on a debt security.

payment obligations on the preferred securities.⁵⁶

ii. Availability of Paragraphs (b) Through (f) to Convertible Debt or Debt-Like Securities

Two commenters addressed whether the modified financial information permitted by paragraphs (b) through (f) should be available for guaranteed debt that is convertible into equity of the parent company, other subsidiaries, or other companies.⁵⁷ The modified financial information permitted by paragraphs (b) through (f) will be available for guaranteed convertible securities only where those securities are convertible into equity securities of the parent company.⁵⁸ If the securities were convertible into securities of a company other than the parent company, the subsidiary issuer would not be considered 100% owned.

c. Availability of Modified Financial Information for Guaranteed Securities Not Described in This Release

The modified financial information permitted by paragraphs (b) through (f) of Rule 3-10 will not be available for every offering of a guaranteed security; they are intended to address only those situations where we are certain that modified financial information is appropriate. We do not believe that, as one commenter suggested, those paragraphs should be available broadly for "any other security if the amounts payable or the other obligations owing to the holder thereunder will not depend on the financial health, value, or performance of the subsidiary issuer or subsidiary guarantor."⁵⁹ However, there may be unique factual situations in which modified financial information would be appropriate, even though those situations are not identified in paragraphs (b) through (f) or otherwise described in this release. In these rare situations, we encourage the issuer and guarantor(s) to contact the Division of Corporation Finance to discuss the filing relating to those securities.⁶⁰ Due

⁵⁶ Ordinarily, the issuers of these securities are finance subsidiaries with no operations or assets other than those in connection with the offering of the securities. Therefore, they should look to paragraph (b) of Rule 3-10.

⁵⁷ Comment letters of PricewaterhouseCoopers (May 4, 1999) and Sullivan & Cromwell (May 4, 1999).

⁵⁸ See, e.g., World Access, Inc. NACT Telecommunications, Inc. (October 28, 1998) and PNC Bank Corp., PNC Bancorp, Inc. (April 1, 1996).

⁵⁹ Comment letter of Sullivan & Cromwell (May 4, 1999).

⁶⁰ Similarly, these issuers and guarantors may either apply to the Commission under Section 12(h) of the Exchange Act for an exemption from the Exchange Act reporting requirements or request a

to the specificity and breadth of today's amendments and the guidance provided in this release and the appendices, we anticipate that these requests will be infrequent.

5. Recently Acquired Subsidiary Issuers and Subsidiary Guarantors

A special issue in the financial statement disclosure for issuers and guarantors is the treatment of recently acquired subsidiary issuers and subsidiary guarantors. Because these subsidiaries generally are not included in the consolidated results of the parent company for all periods, condensed consolidating financial information does not effectively present all material financial information to investors.⁶¹

We proposed to require pre-acquisition financial statements for significant, recently acquired subsidiary issuers and subsidiary guarantors until the condensed consolidating financial information reflects adequately their cash flows and results of operations. These separate audited financial statements would be for the subsidiary's most recent fiscal year preceding the acquisition. Unaudited financial statements also would have to be filed for any interim period specified by Rules 3-01 and 3-02 of Regulation S-X.

As proposed, this treatment would have applied to any recently acquired subsidiary issuer or subsidiary guarantor:

- That has not been included in the audited consolidated results of its parent company for at least nine months of the most recent fiscal year; and
- Whose net book value or purchase price, whichever is greater, equals 20% or more of the shareholders' equity of the parent company on a consolidated basis.⁶²

We heard from several commenters on this proposal. While they generally supported the proposal, several commenters questioned the relevance and practicability of the proposed measure of significance.⁶³ A number of

no-action letter from the Division of Corporation Finance.

⁶¹ Before today's amendments, Rule 3-10 and SAB 53 provided no relief for a subsidiary issuer or subsidiary guarantor for periods before its acquisition. Literal application of Rule 3-10 would have required three years of audited financial statements, regardless of the significance of the acquired subsidiary. The staff has permitted registrants to apply the significance tests then in Rule 3-10(b) by analogy, but that practice provided limited relief and created a number of implementation issues.

⁶² This significance test would be computed by using amounts for the subsidiary as of the most recent fiscal year end before the acquisition.

⁶³ See, e.g., comment letters of Arthur Andersen (May 4, 1999), Sullivan & Cromwell (May 4, 1999),

commenters suggested that significance be measured by comparison to the amount of the securities being registered.⁶⁴ One commenter noted that this measure would focus "on the assets and cash flows of the recently acquired guarantor which will be available to satisfy the registered debt and the amount of credit enhancement the subsidiary is adding to the arrangement."⁶⁵ Other commenters noted anomalies that could result if the parent company had negative shareholders' equity.⁶⁶ For example, a parent company's large deficit could render an acquired guarantor insignificant under the proposed test, even though the guarantor may constitute the primary source of cash flows for repayment of the debt. These commenters also noted that comparison to the securities being registered is consistent with current staff practice.

We are adopting the treatment of recently acquired subsidiaries largely as proposed. However, given the comments we received on the significance measure, we have revised that measure. As adopted, the rule calls for significance to be measured by comparing the net book value or purchase price of the subsidiary to the principal amount of the securities being registered.⁶⁷

The rule requires pre-acquisition financial statements in Securities Act registration statements only. Those financial statements are not required in Exchange Act periodic reports.⁶⁸

Commenters also requested that we clarify various matters regarding the implementation and operation of the paragraph relating to recently acquired subsidiaries. These include:

- Whether individually insignificant acquired guarantors must be aggregated;
- Whether the form of the acquisition affects the requirement for financial statements;
- Whether, and when, financial statements are required for very recently acquired, or not yet acquired, guarantors; and
- Whether use of the pooling or purchase method of accounting affects the financial statements to be provided under Rule 3-10(g).

PricewaterhouseCoopers (May 4, 1999), KPMG LLP (May 4, 1999) and Ernst & Young (May 11, 1999).

⁶⁴ See, e.g., comment letters of PricewaterhouseCoopers (May 4, 1999) and KPMG LLP (May 4, 1999).

⁶⁵ Comment letter of PricewaterhouseCoopers (May 4, 1999).

⁶⁶ See, e.g., comment letter of Ernst & Young (May 4, 1999).

⁶⁷ See Rule 3-10(g)(1)(ii).

⁶⁸ See Instruction 4 to Rule 3-10(g)(1).

Many of these issues are similar to issues currently faced by registrants with significant acquired businesses outside the context of a registered offering of guaranteed debt securities. The staff addresses those issues through its normal practice. In these situations, we encourage the issuer and guarantor(s) to contact the Division of Corporation Finance to discuss the filing relating to those securities.

While some of the requested guidance is outside the scope of today's rule-making, we agree that implementation guidance on a number of these matters would be useful. We have included Appendix B to illustrate the operation of the paragraph relating to recently acquired subsidiaries and provide guidance on various implementation issues.

6. Definitions in Rule 3-10

We proposed to define the following four terms in paragraph (h) of Rule 3-10: "wholly owned," "full and unconditional," "annual report," and "quarterly report." We are adopting as proposed the definitions of "full and unconditional," "annual report," and "quarterly report."⁶⁹

As noted previously, we have made two revisions to the proposed definition of "wholly owned," including changing the defined term to "100% owned."⁷⁰

In response to comments, we also have added the following definitions.

- A parent company has no independent assets or operations if each of its total assets, revenues, income from continuing operations before income taxes, and cash flows from operating activities (excluding amounts related to its investment in its consolidated subsidiaries) is less than 3% of the corresponding consolidated amount.⁷¹
- A subsidiary is minor if each of its total assets, stockholders' equity, revenues, income from continuing operations before income taxes, and cash flows from operating activities is less than 3% of the parent company's corresponding consolidated amount. This definition applies to each subsidiary individually and to all subsidiaries in the aggregate.⁷²

⁶⁹ See Rule 3-10(h)(2), (h)(3), and (h)(4).

⁷⁰ See Rule 3-10(h)(1). We discuss the definition of 100% owned in Section III.A.1.a.—"The meaning of 100% owned."

⁷¹ See Rule 3-10(h)(5).

⁷² See Rule 3-10(h)(6). This 3% test has been applied by the staff in the context of condensed consolidating financial information under SAB 53. In no-action letters under SAB 53, the staff has referred to subsidiaries falling below the 3% test as "inconsequential." To avoid confusion with uses of the term "inconsequential" in other parts of the federal securities laws, for example, in Section 10A(b)(1)(B) of the Exchange Act [15 U.S.C. 78j-

- A subsidiary is a finance subsidiary if it has no assets, operations, revenues, or cash flows other than those related to the issuance, administration, and repayment of the security being registered and any other securities guaranteed by its parent.⁷³

- A subsidiary is an operating subsidiary if it is not a finance subsidiary.⁷⁴

For purposes of Rule 3–10, the parent company is the company that:

- Is an issuer or guarantor of the subject securities;⁷⁵

- Is, or as a result of the subject Securities Act registration statement will be, an Exchange Act reporting company; and

- Owns 100%, directly or indirectly, of each subsidiary issuer and/or subsidiary guarantor of the subject security.

The identity of the parent company will vary based on the particular corporate structure. Instead of a definition of parent company in Rule 3–10, which would fail to account for these variations, we have included a number of examples in Appendix C that explain the term.

1(b)(1)(B)), we are using the term “minor.” The 3% test is a numerical threshold for determining when separate presentation of columnar information for specific subsidiaries may be omitted from condensed consolidating financial information under Rule 3–10. The 3% test is not, and should not be construed as, a standard of general materiality for the preparation of consolidated financial statements.

⁷³ See Rule 3–10(h)(7).

⁷⁴ See Rule 3–10(h)(8).

⁷⁵ It would not be appropriate under Rule 3–10 to file, in substitution for the financial statements of the parent company, financial statements of an entity that files Exchange Act reports but is not an issuer or guarantor of the securities being registered. See Note to Rule 3–10(a)(2). As an illustration, assume the following:

- A parent company with no independent assets or operations issues debt securities that are guaranteed by one or more of its subsidiaries, and
- The parent company is a 100%-owned subsidiary of an entity whose common shares are registered under Section 12 of the Exchange Act, but that entity is not a co-issuer or guarantor of the debt securities.

In this situation, the consolidated financial statements of the parent company must be filed for modified financial information of the subsidiary guarantors to be permitted by paragraphs (b) through (f) of Rule 3–10. The financial statements of the Section 12-registered entity do not meet the conditions in paragraphs (b) through (f) of Rule 3–10, even if the financial statements of that entity are virtually identical to those of the parent company, because the security holders cannot enforce payment of the obligation against that entity. Similarly, the financial statements of a subsidiary that is not an issuer or guarantor of the securities cannot be substituted for those of the parent company. This treatment is consistent with staff practice under SAB 53.

7. Instructions for Condensed Consolidating Financial Information Under Rule 3–10

To help ensure meaningful, consistent presentation of the condensed consolidating financial information, we proposed instructions on how to prepare the financial information. We proposed 13 instructions. We have made seven changes to those proposals.

- We combined proposed paragraphs (i)(1) and (i)(2) into one instruction, reflected in paragraph (i)(1).

- One commenter suggested that we clarify the accounting basis to be used for recently acquired entities included in the guarantor/non-guarantor columns in the condensed consolidating financial information. In response to this suggestion, we created new paragraph (i)(4) to clarify that the basis must be “pushed down” to the applicable subsidiary columns to the extent that push down would be required or permitted in separate financial statements of the subsidiary.⁷⁶

- We revised paragraph (i)(5) to clarify which investments in subsidiaries must be presented under the equity method in the subsidiary issuer or subsidiary guarantor columns.

- We added paragraph (i)(6) to clarify that separate columns are required for subsidiary issuers or subsidiary guarantors that are not 100% owned, whose guarantees are not full and unconditional, or whose guarantees are not joint and several with the guarantees of other subsidiaries.

- We added the words “subsidiary issuers and” into paragraph (i)(10) to reflect that both subsidiary issuers and subsidiary guarantors must comply with Rule 4–08(e)(3) of Regulation S–X.⁷⁷

- We combined proposed paragraphs (i)(10), (i)(11), and (i)(12) into one instruction, paragraph (i)(11).

- We added paragraph (i)(12) to clarify that U.S. GAAP reconciling information for the subsidiaries need not duplicate information included elsewhere in the reconciliation of the parent company’s consolidated financial information.

Other than these seven changes, we have adopted the instructions to Rule 3–10 as proposed.

B. Item 310 of Regulation S–B

We proposed to amend Item 310 of Regulation S–B to require small business issuers to include the same financial information as required by

proposed Rule 3–10. One commenter responded to our request for comment on this proposal.⁷⁸ That commenter believed that the standards for large and small businesses should be the same because the likely higher cost to a small business of providing the information is balanced by the likely greater significance of that information. We are adopting Item 310 of Regulation S–B as proposed.⁷⁹

C. Exchange Act Reporting Requirements

1. Exchange Act Rule 12h–5—Exemption From Periodic Reporting for Subsidiary Issuers and Subsidiary Guarantors Where Parent Company Periodic Reports Include Modified Financial Information as Permitted by Paragraphs (b) Through (f) of Rule 3–10

Before today’s amendments, subsidiary issuers or subsidiary guarantors that were not required to include separate financial statements in their Securities Act registration statements would request that the Division of Corporation Finance provide no-action relief from the Exchange Act reporting requirements. The Division of Corporation Finance applied the same analysis to these requests as it applied in considering the appropriate presentation of financial information in Securities Act registration statements. As noted above, the volume of these requests has increased significantly.

We are adopting new Rule 12h–5 to reduce significantly the need for these requests by providing certainty regarding the availability of an exemption from Exchange Act reporting. Rule 12h–5 exempts from Exchange Act reporting:

- Subsidiary issuers or subsidiary guarantors permitted to omit financial statements by paragraphs (b) through (f) of Rule 3–10; and

- Recently acquired subsidiary issuers or subsidiary guarantors that would be permitted to omit financial statements by paragraphs (b) through (f) of Rule 3–10, but are required to provide pre-acquisition financial statements under paragraph (g) of that rule.

The parent company periodic reports must include the modified financial information permitted by paragraphs (b) through (f) of Rule 3–10. The parent company periodic reports must contain

⁷⁸ Comment letter of KPMG LLP (May 4, 1999).

⁷⁹ One commenter asked us to clarify the application of today’s amendments to offerings that are exempt under Regulation A. See, comment letter of Arthur Andersen (May 4, 1999). An issuer conducting an offering in accordance with Regulation A is not affected by today’s amendments, because only Article 2 of Regulation S–X applies to Regulation A offerings.

⁷⁶ Staff Accounting Bulletin 54 discusses “push down” accounting. See Securities Act Release No. SAB 54 (Nov. 3, 1983) [48 FR 51769].

⁷⁷ 17 CFR 210.4–08(e)(3). Rule 4–08(e)(3) relates to limitations on the payment of dividends.

this information for as long as the subject securities are outstanding. These exemptions are the same as what the staff currently provides in its responses to requests from subsidiary issuers and subsidiary guarantors.

Rule 12h-5 automatically exempts these subsidiary issuers and subsidiary guarantors from Exchange Act reporting requirements. As a result, there would be no need for them to request no-action letters from the Division of Corporation Finance.

2. Non-Financial Disclosure in Parent Company Periodic Reports

Under Rule 12h-5, the parent company's Exchange Act reports must include the modified financial information permitted by paragraphs (b) through (f) of Rule 3-10. The parent company's periodic reports need not, however, provide the non-financial disclosure required by the periodic report form for the subsidiary, unless the securities laws otherwise require the parent company to provide information about the subsidiary.

3. When Rule 12h-5 Becomes Available or Ceases To Be Available

We requested comment on what should be required of subsidiaries that no longer qualify for the exemption from Exchange Act reporting under proposed Rule 12h-5 because they no longer satisfy the requirements of paragraphs (b) through (f) of Rule 3-10. We received no response to our request, other than a general suggestion to clarify the procedures for these situations. The following procedures will apply in these situations.

- If Rule 12h-5 is not initially available to a subsidiary because it does not satisfy the requirements of paragraphs (b) through (f) of Rule 3-10, but later fulfills the requirements, that subsidiary may write to the Division of Corporation Finance to request no-action relief.

- If a subsidiary initially meets the requirements of paragraphs (b) through (f) of Rule 3-10 and relies on Rule 12h-5, but later ceases to satisfy those requirements, we encourage that subsidiary to file promptly an Item 5 Form 8-K or a Form 6-K to report this change in circumstance. That subsidiary must begin reporting pursuant to the Exchange Act when it fails to satisfy paragraphs (b) through (f) of Rule 3-10. That is, the subsidiary must file the Exchange Act report for the period during which it ceased to satisfy paragraphs (b) through (f) of Rule 3-10. The subsidiary must present the financial statements that are required by Regulation S-X at the time the report is

due. The subsidiary may not present the modified information that paragraphs (b) through (f) of Rule 3-10 would have allowed it to present for historical periods.

4. Meaning of the Term "Financial Statements" in Rule 12h-5

One commenter suggested that the language in Rule 12h-5 was somewhat ambiguous because it refers to registrants that are permitted to omit "financial statements."⁸⁰ That commenter stated that condensed consolidating statements are one form of financial statements. In an attempt to avoid this confusion, throughout the proposing and adopting release, we have referred to the required presentation of financial information as condensed consolidating financial information, not condensed consolidating financial statements. In addition, Rule 12h-5 states that the exemption is applicable to those persons permitted to omit separate financial statements by Rule 3-10. If an issuer is not in compliance with Rule 3-10, it is not permitted to omit financial statements in accordance with Rule 3-10. Therefore, we have not revised Rule 12h-5 in response to this comment.

5. Rule 12h-5 Does Not Require Exchange Act Reporting When Financial Statements Are Provided Solely in Accordance With Rule 3-10(g)

One commenter suggested that we add language to clarify the operation of Rule 12h-5(b).⁸¹ The commenter expressed concern that Rule 12h-5 could be misinterpreted to require Exchange Act reporting when Rule 3-10(g) requires financial statements. We revised the language in Rule 12h-5(b) to clarify that, in the case of recently acquired subsidiary issuers or subsidiary guarantors, Exchange Act reporting is not required when financial statements are provided under Rule 3-10 solely because the subsidiary was recently acquired.

6. Application of Rule 12h-5 When the Guaranteed Security Is in Default

We requested comment on whether reporting relief should be available when a guaranteed security is in default. We asked if additional disclosures should be required in that circumstance. One commenter stated that it did not believe that the default should result in the loss of a subsidiary issuer's or subsidiary guarantor's Rule 12h-5

reporting relief.⁸² That commenter also stated that, while additional disclosure may be required in the parent's filing when an issuer defaults on a debt security, it is difficult to predetermine and mandate the necessary disclosure. We agree with that commenter. We also believe that requiring additional disclosure in connection with the exemption provided in Rule 12h-5 is not necessary. Thus, a default on the guaranteed security or the guarantee will not result in the loss of a subsidiary issuer's or subsidiary guarantor's Exchange Act reporting relief under Rule 12h-5.

7. Application of Rule 3-10 and Rule 12h-5 to Foreign Parent Companies With Domestic Subsidiary Issuers or Domestic Subsidiary Guarantors

a. Foreign Parent Companies Reporting on Form 20-F

When a parent company is a foreign private issuer that files on Form 20-F, it is not required to file quarterly reports. Rather, it uses Form 6-K to make public in the United States the information that it made public under foreign law, under exchange regulations, or by distributing it to security holders. Absent the exemption provided by Rule 12h-5, a domestic subsidiary of that foreign parent company would be required to file annual and quarterly reports if it guaranteed registered securities or issued registered, guaranteed securities.

When Rule 12h-5 applies, modified financial information must be included in the parent company's periodic reports.

In the case of a foreign parent company filing on Form 20-F, that disclosure would not appear as frequently as when the domestic subsidiary were reporting. Nevertheless, consistent with the staff's historical position and the concepts underlying Rule 3-10, we believe that the parent company in this situation should not be required to file quarterly information regarding the domestic subsidiary. As we believe that the financial statements of the parent company, along with the required modified financial information permitted by Rule 3-10, are sufficient to inform an investment decision in those situations, the required periodic reports for that parent also should be sufficient. Therefore, if the parent company reports on Form 20-F and is not required to file quarterly reports under the Exchange Act, Rule 3-10 would not require that parent company to file more frequent information regarding its domestic

⁸⁰ Comment letter of KPMG LLP (May 4, 1999).

⁸¹ Comment letter of Arthur Andersen (May 4, 1999).

⁸² Comment letter of PricewaterhouseCoopers (May 4, 1999).

subsidiary issuers and domestic subsidiary guarantors.

Rule 3-10(a)(3) states that foreign parent companies should look to Item 8.A of Form 20-F to determine the periods for which financial statements are required. On September 30, 2000, Item 8.A of Form 20-F will replace Rule 3-19 of Regulation S-X as the source for the financial statement requirements for foreign private issuers.⁸³ Before September 30, 2000, foreign private issuers should look to Rule 3-19 instead of Item 8A.

b. Foreign Parent Companies Reporting on Form 40-F

When a Canadian parent company and one or more subsidiaries register an offering of guaranteed securities under the multijurisdictional disclosure system, the parent company and the subsidiaries incur reporting obligations under Section 15(d).⁸⁴ When a subsidiary issuer or subsidiary guarantor is also eligible to register its security under the MJDS,⁸⁵ the financial statements that would appear in the registration statement and in any annual report on Form 40-F⁸⁶ filed by the Canadian parent company would not be affected by Rule 3-10. The disclosure would be in accordance with Canadian disclosure standards. When a subsidiary issuer or subsidiary guarantor is not eligible to register its security under the MJDS,⁸⁷ the financial statements of the parent company included in the Securities Act registration statement and an Exchange Act registration statement or annual must comply with Rule 3-10.

D. Financial Statements of Affiliates Whose Securities Collateralize Registered Securities—Rule 3-16 of Regulation S-X

Before today's amendments, the financial statement requirements for affiliates whose securities collateralize registered securities were combined

with the requirements for guarantors in Rule 3-10 of Regulation S-X. Because the amendments to Rule 3-10 change significantly the structure of that rule, we are moving the requirements for these affiliates into a rule that applies only to them—Rule 3-16 of Regulation S-X. This change will avoid confusion and make the requirements easier to follow. We are merely relocating the financial statement requirements for affiliates whose securities collateralize registered securities to Rule 3-16; we are not changing those requirements in any way.⁸⁸

One commenter suggested that we clarify whether small business issuers must comply with new Rule 3-16 of Regulation S-X.⁸⁹ In response to this comment, we have made clear in Regulation S-B that small business issuers also must comply with Rule 3-16.⁹⁰

One commenter asked us to clarify whether a collateralizing affiliate incurs Exchange Act reporting obligations.⁹¹ Consistent with the past approach, we confirm that collateralizing affiliates will continue not to incur Exchange Act reporting requirements.

Similarly, one commenter asked us to clarify whether financial statements of collateralizing affiliates are required in quarterly reports of the issuer of the collateralized security.⁹² Unlike subsidiary issuers and subsidiary guarantors, collateralizing affiliates are not registrants.⁹³ Therefore, financial statements of collateralizing affiliates are not required in quarterly reports of the issuer of the collateralized security.

IV. Phase-In of Today's Amendments to Rule 3-10

To ease the transition to the amendments to Rule 3-10, we will use the following phase-in schedule.

For Securities Act registration statements:

- Any registration statement that is first filed on or after September 25, 2000 must comply with amended Rule 3-10; and

- Any post-effective amendment filed on or after September 25, 2000 to include either the company's latest audited financial statements in the registration statement or to update the prospectus under Section 10(a)(3) must comply with amended Rule 3-10. For Exchange Act registration statements:

- Any registration statement that is first filed on or after September 25, 2000 must comply with amended Rule 3-10. For Exchange Act periodic reports:

- If the reporting company was required to comply with amended Rule 3-10 in a Securities Act or Exchange Act registration statement, all Exchange Act periodic reports for periods ending after that registration statement became effective must comply with amended Rule 3-10;

- For all other reporting companies, the annual report on Form 10-K, Form 10-KSB, or Form 20-F, as applicable, for the first fiscal year ending after [effective date] must comply with amended Rule 3-10 and all Exchange Act periodic reports for subsequent periods must comply with amended Rule 3-10.

In the first registration statement or periodic report to which amended Rule 3-10 applies, the financial statements must reflect the application of amended Rule 3-10 for all periods presented.

V. Cost-Benefit Analysis

We are adopting financial reporting rules for related issuers and guarantors of guaranteed securities. We are also adopting an exemption from periodic reporting for subsidiary issuers and subsidiary guarantors. For the most part, today's amendments codify the positions the staff has developed through Staff Accounting Bulletin No. 53, later interpretations, and the registration statement review process. The amendments deviate from current practice in a significant way only in the following two situations:

- An operating subsidiary issues securities, its parent guarantees the securities, and no subsidiary guarantees the securities; and
- A parent issues securities, an operating subsidiary guarantees the securities, and no other subsidiary guarantees the securities.

Under SAB 53, the staff continued to permit those subsidiaries to present summarized financial information instead of full financial statements. Under the amendments, those

⁸³ 17 CFR 210.3-19.

⁸⁴ The multijurisdictional disclosure system, or MJDS, is a cross-border securities registration and reporting arrangement that we have established with securities regulators in Canada. It is comprised of Forms F-7, F-8, F-9, F-10 and F-80 under the Securities Act and Form 40-F under the Exchange Act. Companies registering securities under Forms F-7, F-8 and F-80 may avoid the reporting obligations under Section 15(d). See, Exchange Act Rule 12h-4.

⁸⁵ General Instruction I.E of Form F-9 and General Instruction I.H of Form F-10 permit majority-owned subsidiaries to register securities on those forms if various conditions are met.

⁸⁶ 17 CFR 249.240f.

⁸⁷ This situation arises when the subsidiary issuer or subsidiary guarantor is not incorporated in Canada. In this situation, registrants have filed the registration statement on a combined Form F-9/S-3 or Form F-10/S-1, depending on what registration form the subsidiary is eligible to use.

⁸⁸ We have amended Instruction 1 to Item 8 of Form 20-F to include a reference to new Rule 3-16. This amendment merely recognizes that we have moved the requirements for affiliates whose securities collateralize registered securities; it does not change the financial statement requirements in Form 20-F.

⁸⁹ Comment letter of Arthur Andersen (May 4, 1999).

⁹⁰ See, Note 4 to Item 310 of Regulation S-B.

⁹¹ Comment letter of Arthur Andersen (May 4, 1999).

⁹² Comment letter of Arthur Andersen (May 4, 1999).

⁹³ Rule 10-01(a)(1) of Regulation S-X [17 CFR 210.10-01(a)(1)] states "Interim financial statements required by this rule need only be provided as to the registrant and its subsidiaries consolidated and may be unaudited. Separate statements of other entities which may otherwise be required by this regulation may be omitted."

subsidiaries will be required to present condensed consolidating financial information instead of summarized financial information.

We believe that condensed consolidating financial information is more appropriate than summarized financial information, as it more clearly distinguishes the assets, liabilities, revenues, expenses, and cash flows of the entities that are legally obligated under the indenture from those that are not.⁹⁴ Furthermore, condensed consolidating financial information provides the same level of detail about the financial position, results of operations, and cash flows of subsidiary issuers and subsidiary guarantors that investors are accustomed to obtaining in interim financial statements of a registrant. It also facilitates analysis of trends affecting subsidiary issuers and subsidiary guarantors and relationships among the various components of a consolidated organization.

For purposes of this cost-benefit analysis, there is one quantifiable cost and one quantifiable benefit for registrants. The quantifiable cost is that of preparing condensed consolidating financial information in those situations in which they could have prepared only summarized financial information previously. The quantifiable benefit is the savings to be recognized by not having to prepare a request for relief from the reporting requirements of the Exchange Act. We estimate the total cost to be \$87,000 annually. We estimate the total benefit to be \$850,000 annually.⁹⁵

In the proposing release, we estimated the aggregate additional annual cost to each registrant that would have to switch from summarized financial information to condensed consolidating financial information to be approximately \$1,000. In that release, we also stated that there were 29 registrants that had received a no-action letter in calendar year 1998 from the Division of Corporation Finance permitting them to include summarized financial information in lieu of separate financial statements. In calendar year 1999, there were 26 such registrants. Based on the 1998 numbers, we estimated the total annual cost of the amendments to be \$29,000.

We requested comment on our estimates. Two commenters felt that our

⁹⁴ Summarized financial information may obscure these distinctions, particularly if subsidiary guarantors themselves have consolidated operating subsidiaries that are not guarantors.

⁹⁵ See Securities Act Release No. 7649 (March 5, 1999) [64 FR 10579], § VIII.

estimates were too low.⁹⁶ We discuss these comments below.

One commenter suggested that it would cost an average of \$25,000 to prepare condensed consolidating financial information.⁹⁷ That commenter, however, did not provide us with an estimate of how much more it would cost to provide condensed consolidating financial information rather than summarized financial information. We have, therefore, not revised our estimates in response to this comment.

One commenter felt that, for those registrants that would have to switch from summarized financial information to condensed consolidating financial information, it was unreasonable to look at their increased costs for one year instead of the number of years they would provide condensed consolidating financial information. Based on this comment, we have considered the total cost to each registrant to be \$1,000 for each of the three years for which financial information is generally required.⁹⁸ This results in a cost to each such registrant of \$3,000.

Using the revised cost estimate of \$3,000, the 29 registrants that received a no-action letter in calendar year 1998 from the Division of Corporation Finance permitting them to include summarized financial information in lieu of separate financial statements would have an increased cost of \$87,000. The cost for the 26 registrants that were in that position based on 1999 no-action letters would be \$78,000.

Today's amendments benefit companies by reducing the need to prepare and submit requests for no-action letters from the Division of Corporation Finance. In the proposing release, we estimated the annual savings to registrants to be approximately \$850,000.⁹⁹ In that release, we also discussed the manner in which we estimated those annual savings. There were no responses to our request for

⁹⁶ Comment letters of KPMG LLP (May 4, 1999) and Reynolds Metals Company (May 4, 1999).

⁹⁷ Comment letter of KPMG LLP (May 4, 1999).

⁹⁸ The financial statement requirements for registrants that are not small business issuers are contained in Regulation S-X [17 CFR 210.1-01 through 12-29]. The financial statement requirements for small business issuers are contained in Item 310 of Regulation S-B [17 CFR 228.310].

⁹⁹ There were 130 no-action letters issued by the Division of Corporation Finance regarding SAB 53 in 1999. The financial information requirements under today's amendments would be the same with respect to 104 of the no-action letters. The financial information requirements under today's amendments would result in condensed consolidating financial information instead of summarized financial information with respect to 26 of the no-action letters.

comment on the reasonableness of our savings estimates.

In addition to the quantifiable benefit of today's amendments to registrants, we believe that there also are a significant number of unquantifiable benefits to registrants and investors, including the following:

- Today's amendments eliminate uncertainty about which financial statements and periodic reports subsidiary issuers and subsidiary guarantors must file;
- Today's amendments require financial information that is more helpful to an investor in the two areas where summarized financial statements are permitted today;¹⁰⁰ and
- Because registrants are required to provide condensed consolidating financial information in all situations in which they must provide separate financial information, investors will be able to compare the financial information among all offerings and in the secondary markets.

VI. Effects on Efficiency, Competition, and Capital Formation

As required by Section 23(a) of the Exchange Act,¹⁰¹ we considered the impact any new Exchange Act rule would have on competition. We requested comment on the proposals, but received no response to our request for comment. We believe that the amendments will not have any anti-competitive effect since the rules, to a large extent, simply codify the reporting requirements to which registrants are already subject.

In addition, Section 2(b) of the Securities Act¹⁰² and Section 3(f) of the Exchange Act¹⁰³ require us, in adopting a rule that requires a public interest finding, to consider whether the proposed rule will promote efficiency, competition and capital formation. We sought comment on how these changes would affect competition, capital formation and market efficiency, but received no response to our request for comment. We believe that the amendments will have a positive, but

¹⁰⁰ Condensed consolidating financial information requires the columnar presentation of each category of parent and subsidiary as issuer, guarantor, or non-guarantor. This approach more clearly distinguishes the assets, liabilities, revenues, expenses, and cash flows of the entities that are legally obligated under the indenture from those that are not, particularly if subsidiary guarantors themselves have consolidated operating subsidiaries that are not guarantors. Another important element of credit decisions is cash flow information. Condensed consolidating financial information requires this information while summarized financial information does not.

¹⁰¹ 15 U.S.C. 78w(a).

¹⁰² 15 U.S.C. 78b(b).

¹⁰³ 15 U.S.C. 78c(f).

unquantifiable, effect on efficiency, competition, and capital formation. The use of condensed consolidating financial information will help investors assess better the repayment risk of different issuers.

We find that the exemptions under Sections 7¹⁰⁴ and 28¹⁰⁵ of the Securities Act and Sections 12(h) and 36¹⁰⁶ of the Exchange Act are in the public interest and for the protection of investors.

VII. Final Regulatory Flexibility Act Certification

In connection with the rule proposals, the Chairman of the Commission certified that the proposed amendments would not, if adopted, have a significant economic impact on a substantial number of small entities. The certification, including the factual bases for the determination, was published with the proposing release in satisfaction of Section 605(b) of Regulatory Flexibility Act.¹⁰⁷ We requested comments on the certification, but received none.

VIII. Paperwork Reduction Act

We submitted to the Office of Management and Budget the proposals for review in accordance with the Paperwork Reduction Act of 1995.¹⁰⁸ The amendments will affect the inclusion of information in Securities Act registration Forms S-1, F-1, S-4 and F-4 (OMB control numbers 3235-0065, 3235-0258, 3235-0324, and 3235-0325, respectively). We estimated that the proposed rules would increase the average burden per form by approximately five minutes.¹⁰⁹ The amendments will also affect the inclusion of information in Exchange Act Forms 10, 10-SB, 10-K, 10-KSB, 10-Q, 10-QSB and 20-F (OMB control numbers 3235-0064, 3235-0063, 3235-0070 and 3235-0288).¹¹⁰ We estimated the proposed rules would increase the

average burden per form by approximately three minutes for Form 10-K, one minute for Form 10-Q, five minutes for Form 10 and one minute for Form 20-F.¹¹¹ We estimated the increased burden hours for each form by dividing the estimated aggregate increased burden for all forms, whether or not the filers would be required to report under Rule 3-10, by the estimated total number of filers. The burden for Regulation S-X (OMB control number 3235-0009) will remain unchanged.

The amendments will not affect the retention period. The filing of financial statements, as described in this release, is mandatory. They are not kept confidential. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a correctly valid control number.

No commenter responded to our request for comment with respect to these proposed changes in burden hours for each affected form.

IX. Statutory Bases

The rule amendments outlined above are proposed pursuant to Sections 7, 10,¹¹² 19(a),¹¹³ and 28 of the Securities Act and Sections 3(b), 12,¹¹⁴ 13,¹¹⁵ 15(d),¹¹⁶ 23,¹¹⁷ and 36 of the Exchange Act.

¹¹¹ To arrive at this number for Form 10-K, we divided the estimated number of companies that will have to provide condensed consolidating financial information in lieu of summarized financial information per year (29) by the estimated number of filings on this form per year (10,392) and multiplied that quotient (.00279) by the estimated number of hours to convert financials (16). To arrive at this number for Form 10-Q, we divided the estimated number of companies that will have to provide condensed consolidating financial information in lieu of summarized financial information per year (29) by the estimated number of filings on this form per year (10,392) and multiplied that quotient (.00279) by the estimated number of hours to convert financials (16). To arrive at this number for Form 10, we divided the estimated number of companies that will have to provide condensed consolidating financial information in lieu of summarized financial information per year (29) by the estimated number of filings on this form per year (124) and multiplied that quotient (.0056451) by the estimated number of hours to convert financials (16). To arrive at this number for Form 20-F, we divided the estimated number of companies that will have to provide condensed consolidating financial information in lieu of summarized financial information per year (1.7) by the estimated number of filings on this form per year (1,007) and multiplied that quotient (.0015888) by the estimated number of hours to convert financials (16).

¹¹² 15 U.S.C. 77j.

¹¹³ 15 U.S.C. 77t.

¹¹⁴ 15 U.S.C. 78l.

¹¹⁵ 15 U.S.C. 78m.

¹¹⁶ 15 U.S.C. 78o(d).

¹¹⁷ 15 U.S.C. 78w.

List of Subjects

17 CFR Parts 210 and 211

Accounting, Reporting and recordkeeping requirements, Securities.

17 CFR Part 228

Reporting and recordkeeping requirements, Securities, Small Businesses.

17 CFR Part 240

Reporting and recordkeeping requirements, Securities.

17 CFR Part 249

Brokers, Reporting and recordkeeping requirements, Securities.

Text of the Amendments

For the reasons set out in the preamble, the Securities and Exchange Commission amends title 17, chapter II of the Code of Federal Regulations as follows:

PART 210—FORM AND CONTENT OF AND REQUIREMENTS FOR FINANCIAL STATEMENTS, SECURITIES ACT OF 1933, SECURITIES EXCHANGE ACT OF 1934, PUBLIC UTILITY HOLDING COMPANY ACT OF 1935, INVESTMENT COMPANY ACT OF 1940, AND ENERGY POLICY AND CONSERVATION ACT OF 1975

1. The authority citation for Part 210 continues to read as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z-2, 77aa(25), 77aa(26), 78j-i, 78l, 78m, 78n, 78o(d), 78u-5, 78w(a), 78ll(d), 79e(b), 79j(a), 79n, 79t(a), 80a-8, 80a-20, 80a-29, 80a-30, 80a-37(a), unless otherwise noted.

2. Section 210.3-10 is revised to read as follows:

§ 210.3-10 Financial statements of guarantors and issuers of guaranteed securities registered or being registered.

(a)(1) *General rule.* Every issuer of a registered security that is guaranteed and every guarantor of a registered security must file the financial statements required for a registrant by Regulation S-X.

(2) *Operation of this rule.* Paragraphs (b), (c), (d), (e) and (f) of this section are exceptions to the general rule of paragraph (a)(1) of this section. Only one of these paragraphs can apply to a single issuer or guarantor. Paragraph (g) of this section is a special rule for recently acquired issuers or guarantors that overrides each of these exceptions for a specific issuer or guarantor. Paragraph (h) of this section defines the following terms used in this section: 100% owned, full and unconditional, annual report, quarterly report, no

¹⁰⁴ 15 U.S.C. 77g.

¹⁰⁵ 15 U.S.C. 77z-3.

¹⁰⁶ 15 U.S.C. 78mm.

¹⁰⁷ 5 U.S.C. 605(b).

¹⁰⁸ 44 U.S.C. § 3501 *et seq.*

¹⁰⁹ To arrive at this number, we divided the estimated number of companies that will have to provide condensed consolidating financial information in lieu of summarized financial information per year (29) by the estimated number of filings on these forms per year (5,653) and multiplied that quotient (.00513) by the estimated number of hours to convert financials (16).

¹¹⁰ In the last ten years, the Division of Corporation Finance has responded to only one SAB 53 request in which the related offering was registered on a small business issuer form. Given the size of issuers who generally issue guaranteed debt, we do not expect that filers on Forms 10-SB, 10-QSB and 10-KSB are likely to issue such debt. Therefore, we make no changes with respect to these forms.

independent assets or operations, minor, finance subsidiary and operating subsidiary. Paragraph (i) of this section states the requirements for preparing the condensed consolidating financial information required by paragraphs (c), (d), (e) and (f) of this section.

Note to paragraph (a)(2). Where paragraphs (b), (c), (d), (e) and (f) of this section specify the filing of financial statements of the parent company, the financial statements of an entity that is not an issuer or guarantor of the registered security cannot be substituted for those of the parent company.

(3) *Foreign private issuers.* Where any provision of this section requires compliance with §§ 210.3-01 and 3-02, a foreign private issuer may comply by providing financial statements for the periods specified by Item 8.A of Form 20-F (§ 249.220f of this chapter).

(b) *Finance subsidiary issuer of securities guaranteed by its parent company.* When a finance subsidiary issues securities and its parent company guarantees those securities, the registration statement, parent company annual report, or parent company quarterly report need not include financial statements of the issuer if:

(1) The issuer is 100% owned by the parent company guarantor;

(2) The guarantee is full and unconditional;

(3) No other subsidiary of the parent company guarantees the securities; and

(4) The parent company's financial statements are filed for the periods specified by §§ 210.3-01 and 210.3-02 and include a footnote stating that the issuer is a 100%-owned finance subsidiary of the parent company and the parent company has fully and unconditionally guaranteed the securities. The footnote also must include the narrative disclosures specified in paragraphs (i)(9) and (i)(10) of this section.

Note to paragraph (b). Paragraph (b) is available if a subsidiary issuer satisfies the requirements of this paragraph but for the fact that, instead of the parent company guaranteeing the security, the subsidiary issuer co-issued the security, jointly and severally, with the parent company. In this situation, the narrative information required by paragraph (b)(4) must be modified accordingly.

(c) *Operating subsidiary issuer of securities guaranteed by its parent company.* When an operating subsidiary issues securities and its parent company guarantees those securities, the registration statement, parent company annual report, or parent company quarterly report need not include financial statements of the issuer if:

(1) The issuer is 100% owned by the parent company guarantor;

(2) The guarantee is full and unconditional;

(3) No other subsidiary of the parent company guarantees the securities; and

(4) The parent company's financial statements are filed for the periods specified by §§ 210.3-01 and 210.3-02 and include, in a footnote, condensed consolidating financial information for the same periods with a separate column for:

(i) The parent company;

(ii) The subsidiary issuer;

(iii) Any other subsidiaries of the parent company on a combined basis;

(iv) Consolidating adjustments; and

(v) The total consolidated amounts.

Notes to paragraph (c).

1. Instead of the condensed consolidating financial information required by paragraph (c)(4), the parent company's financial statements may include a footnote stating, if true, that the parent company has no independent assets or operations, the guarantee is full and unconditional, and any subsidiaries of the parent company other than the subsidiary issuer are minor. The footnote also must include the narrative disclosures specified in paragraphs (i)(9) and (i)(10) of this section.

2. If the alternative disclosure permitted by Note 1 to this paragraph is not applicable because the parent company has independent assets or operations, the condensed consolidating financial information described in paragraph (c)(4) may omit the column for "any other subsidiaries of the parent company on a combined basis" if those other subsidiaries are minor.

3. Paragraph (c) is available if a subsidiary issuer satisfies the requirements of this paragraph but for the fact that, instead of the parent company guaranteeing the security, the subsidiary issuer co-issued the security, jointly and severally, with the parent company. In this situation, the narrative information required by paragraph (i)(8) of this section must be modified accordingly.

(d) *Subsidiary issuer of securities guaranteed by its parent company and one or more other subsidiaries of that parent company.* When a subsidiary issues securities and both its parent company and one or more other subsidiaries of that parent company guarantee those securities, the registration statement, parent company annual report, or parent company quarterly report need not include financial statements of the issuer or any subsidiary guarantor if:

(1) The issuer and all subsidiary guarantors are 100% owned by the parent company guarantor;

(2) The guarantees are full and unconditional;

(3) The guarantees are joint and several; and

(4) The parent company's financial statements are filed for the periods

specified by §§ 210.3-01 and 210.3-02 and include, in a footnote, condensed consolidating financial information for the same periods with a separate column for:

(i) The parent company;

(ii) The subsidiary issuer;

(iii) The guarantor subsidiaries of the parent company on a combined basis;

(iv) Any other subsidiaries of the parent company on a combined basis;

(v) Consolidating adjustments; and

(vi) The total consolidated amounts.

Notes to paragraph (d).

1. Paragraph (d) applies in the same manner whether the issuer is a finance subsidiary or an operating subsidiary.

2. The condensed consolidating financial information described in paragraph (d)(4) may omit the column for "any other subsidiaries of the parent company on a combined basis" if those other subsidiaries are minor.

3. Paragraph (d) is available if a subsidiary issuer satisfies the requirements of this paragraph but for the fact that, instead of the parent company guaranteeing the security, the subsidiary issuer co-issued the security, jointly and severally, with the parent company. In this situation, the narrative information required by paragraph (i)(8) of this section must be modified accordingly.

4. If all of the requirements in paragraph (d) are satisfied except that the guarantee of a subsidiary is not joint and several with, as applicable, the parent company's guarantee or the guarantees of the parent company and the other subsidiaries, then each subsidiary guarantor whose guarantee is not joint and several need not include separate financial statements, but the condensed consolidating financial information should include a separate column for each guarantor whose guarantee is not joint and several.

5. Instead of the condensed consolidating financial information required by paragraph (d)(4), the parent company's financial statements may include a footnote stating, if true, that the parent company has no independent assets or operations, the subsidiary issuer is a 100% owned finance subsidiary of the parent company, the parent company has guaranteed the securities, all of the parent company's subsidiaries other than the subsidiary issuer have guaranteed the securities, all of the guarantees are full and unconditional, and all of the guarantees are joint and several. The footnote also must include the narrative disclosures specified in paragraphs (i)(9) and (i)(10) of this section.

(e) *Single subsidiary guarantor of securities issued by the parent company of that subsidiary.* When a parent company issues securities and one of its subsidiaries guarantees those securities, the registration statement, parent company annual report, or parent company quarterly report need not include financial statements of the subsidiary guarantor if:

(1) The subsidiary guarantor is 100% owned by the parent company issuer;

(2) The guarantee is full and unconditional;

(3) No other subsidiary of that parent guarantees the securities; and

(4) The parent company's financial statements are filed for the periods specified by §§ 210.3-01 and 210.3-02 and include, in a footnote, condensed consolidating financial information for the same periods with a separate column for:

- (i) The parent company;
- (ii) The subsidiary guarantor;
- (iii) Any other subsidiaries of the parent company on a combined basis;
- (iv) Consolidating adjustments; and
- (v) The total consolidated amounts.

Notes to paragraph (e).

1. Paragraph (e) applies in the same manner whether the guarantor is a finance subsidiary or an operating subsidiary.

2. Instead of the condensed consolidating financial information required by paragraph (e)(4), the parent company's financial statements may include a footnote stating, if true, that the parent company has no independent assets or operations, the guarantee is full and unconditional, and any subsidiaries of the parent company other than the subsidiary guarantor are minor. The footnote also must include the narrative disclosures specified in paragraphs (i)(9) and (i)(10) of this section.

3. If the alternative disclosure permitted by Note 2 to this paragraph is not applicable because the parent company has independent assets or operations, the condensed consolidating financial information described in paragraph (e)(4) may omit the column for "any other subsidiaries of the parent company on a combined basis" if those other subsidiaries are minor.

4. If, instead of guaranteeing the subject security, a subsidiary co-issues the security jointly and severally with its parent company, this paragraph (e) does not apply. Instead, the appropriate financial information requirement would depend on whether the subsidiary is a finance subsidiary or an operating subsidiary. If the subsidiary is a finance subsidiary, paragraph (b) applies. If the subsidiary is an operating company, paragraph (c) applies.

(f) *Multiple subsidiary guarantors of securities issued by the parent company of those subsidiaries.* When a parent company issues securities and more than one of its subsidiaries guarantee those securities, the registration statement, parent company annual report, or parent company quarterly report need not include financial statements of the subsidiary guarantors if:

- (1) Each of the subsidiary guarantors is 100% owned by the parent company issuer;
- (2) The guarantees are full and unconditional;
- (3) The guarantees are joint and several; and

(4) The parent company's financial statements are filed for the periods specified by §§ 210.3-01 and 210.3-02 and include, in a footnote, condensed consolidating financial information for the same periods with a separate column for:

- (i) The parent company;
- (ii) The subsidiary guarantors on a combined basis;
- (iii) Any other subsidiaries of the parent company on a combined basis;
- (iv) Consolidating adjustments; and
- (v) The total consolidated amounts.

Notes to paragraph (f).

1. Instead of the condensed consolidating financial information required by paragraph (f)(4), the parent company's financial statements may include a footnote stating, if true, that the parent company has no independent assets or operations, the guarantees are full and unconditional and joint and several, and any subsidiaries of the parent company other than the subsidiary guarantors are minor. The footnote also must include the narrative disclosures specified in paragraphs (i)(9) and (i)(10) of this section.

2. If the alternative disclosure permitted by Note 1 to this paragraph is not applicable because the parent company has independent assets or operations, the condensed consolidating financial information described in paragraph (f)(4) may omit the column for "any other subsidiaries of the parent company on a combined basis" if those other subsidiaries are minor.

3. If any of the subsidiary guarantees is not joint and several with the guarantees of the other subsidiaries, then each subsidiary guarantor whose guarantee is not joint and several need not include separate financial statements, but the condensed consolidating financial information must include a separate column for each subsidiary guarantor whose guarantee is not joint and several.

(g) *Recently acquired subsidiary issuers or subsidiary guarantors.*

(1) The Securities Act registration statement of the parent company must include the financial statements specified in paragraph (g)(2) of this section for any subsidiary that otherwise meets the conditions in paragraph (c), (d), (e) or (f) of this section for omission of separate financial statements if:

- (i) The subsidiary has not been included in the audited consolidated results of the parent company for at least nine months of the most recent fiscal year; and
- (ii) The net book value or purchase price, whichever is greater, of the subsidiary is 20% or more of the principal amount of the securities being registered.

(2) Financial statements required.

(i) Audited financial statements for a subsidiary described in paragraph (g)(1) of this section must be filed for the subsidiary's most recent fiscal year preceding the acquisition. In addition,

unaudited financial statements must be filed for any interim periods specified in §§ 210.3-01 and 210.3-02.

(ii) The financial statements must conform to the requirements of Regulation S-X (§§ 210.1-01 through 12-29), except that supporting schedules need not be filed. If the subsidiary is a foreign business, financial statements of the subsidiary meeting the requirements of Item 17 of Form 20-F (§ 249.220f) will satisfy this item.

(3) Instructions to paragraph (g).

(i) The significance test of paragraph (g)(1)(ii) of this section should be computed using net book value of the subsidiary as of the most recent fiscal year end preceding the acquisition.

(ii) Information required by this paragraph (g) is not required to be included in an annual report or quarterly report.

(iii) Acquisitions of a group of subsidiary issuers or subsidiary guarantors that are related prior to their acquisition shall be aggregated for purposes of applying the 20% test in paragraph (g)(1)(ii) of this section. Subsidiaries shall be deemed to be related prior to their acquisition if:

(A) They are under common control or management;

(B) The acquisition of one subsidiary is conditioned on the acquisition of each subsidiary; or

(C) The acquisition of each subsidiary is conditioned on a single common event.

(h) *Definitions.* For the purposes of this section:

(1) A subsidiary is "100% owned" if all of its outstanding voting shares are owned, either directly or indirectly, by its parent company. A subsidiary not in corporate form is 100% owned if the sum of all interests are owned, either directly or indirectly, by its parent company other than:

- (i) Securities that are guaranteed by its parent and, if applicable, other 100%-owned subsidiaries of its parent; and
- (ii) Securities that guarantee securities issued by its parent and, if applicable, other 100%-owned subsidiaries of its parent.

(2) A guarantee is "full and unconditional," if, when an issuer of a guaranteed security has failed to make a scheduled payment, the guarantor is obligated to make the scheduled payment immediately and, if it doesn't, any holder of the guaranteed security may immediately bring suit directly against the guarantor for payment of all amounts due and payable.

(3) *Annual report* refers to an annual report on Form 10-K, Form 10-KSB, or

Form 20-F (§§ 249.310, 249.310b, or 249.220f of this chapter).

(4) *Quarterly report* refers to a quarterly report on Form 10-Q or Form 10-QSB (§§ 249.308a or 249.308b of this chapter).

(5) A parent company has no independent assets or operations if each of its total assets, revenues, income from continuing operations before income taxes, and cash flows from operating activities (excluding amounts related to its investment in its consolidated subsidiaries) is less than 3% of the corresponding consolidated amount.

(6) A subsidiary is minor if each of its total assets, stockholders' equity, revenues, income from continuing operations before income taxes, and cash flows from operating activities is less than 3% of the parent company's corresponding consolidated amount.

Note to paragraph (h)(6). When considering a group of subsidiaries, the definition applies to each subsidiary in that group individually and to all subsidiaries in that group in the aggregate.

(7) A subsidiary is a finance subsidiary if it has no assets, operations, revenues or cash flows other than those related to the issuance, administration and repayment of the security being registered and any other securities guaranteed by its parent company.

(8) A subsidiary is an operating subsidiary if it is not a finance subsidiary.

(i) Instructions for preparation of the condensed consolidating financial information required by paragraphs (c), (d), (e) and (f) of this section.

(1) Follow the general guidance in § 210.10-01 for the form and content for condensed financial statements and present the financial information in sufficient detail to allow investors to determine the assets, results of operations and cash flows of each of the consolidating groups;

(2) The financial information should be audited for the same periods that the parent company financial statements are required to be audited;

(3) The parent company column should present investments in all subsidiaries under the equity method;

(4) The parent company's basis shall be "pushed down" to the applicable subsidiary columns to the extent that push down would be required or permitted in separate financial statements of the subsidiary;

(5) All subsidiary issuer or subsidiary guarantor columns should present the following investments in subsidiaries under the equity method:

(i) Non-guarantor subsidiaries;

(ii) Subsidiary issuers or subsidiary guarantors that are not 100% owned or whose guarantee is not full and unconditional;

(iii) Subsidiary guarantors whose guarantee is not joint and several with the guarantees of the other subsidiaries; and

(iv) Subsidiary guarantors with differences in domestic or foreign laws that affect the enforceability of the guarantees;

(6) Provide a separate column for each subsidiary issuer or subsidiary guarantor that is not 100% owned, whose guarantee is not full and unconditional, or whose guarantee is not joint and several with the guarantees of other subsidiaries. Inclusion of a separate column does not relieve that issuer or guarantor from the requirement to file separate financial statements under paragraph (a) of this section. However, paragraphs (b) through (f) of this section will provide this relief if the particular paragraph is satisfied except that the guarantee is not joint and several;

(7) Provide separate columns for each guarantor by legal jurisdiction if differences in domestic or foreign laws affect the enforceability of the guarantees;

(8) Include the following disclosure, if true:

(i) Each subsidiary issuer or subsidiary guarantor is 100% owned by the parent company;

(ii) All guarantees are full and unconditional; and

(iii) Where there is more than one guarantor, all guarantees are joint and several;

(9) Disclose any significant restrictions on the ability of the parent company or any guarantor to obtain funds from its subsidiaries by dividend or loan;

(10) Provide the disclosures prescribed by § 210.4-08(e)(3) with respect to the subsidiary issuers and subsidiary guarantors;

(11) The disclosure:

(i) May not omit any financial and narrative information about each guarantor if the information would be material for investors to evaluate the sufficiency of the guarantee;

(ii) Shall include sufficient information so as to make the financial information presented not misleading; and

(iii) Need not repeat information that would substantially duplicate disclosure elsewhere in the parent company's consolidated financial statements; and

(12) Where the parent company's consolidated financial statements are prepared on a comprehensive basis other than U.S. Generally Accepted Accounting Principles, reconcile the information in each column to U.S. Generally Accepted Accounting Principles to the extent necessary to allow investors to evaluate the sufficiency of the guarantees. The reconciliation may be limited to the information specified by Item 17 of Form 20-F (§ 249.220f of this chapter). The reconciling information need not duplicate information included elsewhere in the reconciliation of the consolidated financial statements.

3. Section 210.3-16 is added to read as follows:

§ 210.3-16 Financial statements of affiliates whose securities collateralize an issue registered or being registered.

(a) For each of the registrant's affiliates whose securities constitute a substantial portion of the collateral for any class of securities registered or being registered, there shall be filed the financial statements that would be required if the affiliate were a registrant

and required to file financial statements. However, financial statements need not be filed pursuant to this section for any person whose statements are otherwise separately included in the filing on an individual basis or on a basis consolidated with its subsidiaries.

(b) For the purposes of this section, securities of a person shall be deemed to constitute a substantial portion of collateral if the aggregate principal amount, par value, or book value of the securities as carried by the registrant, or the market value of such securities, whichever is the greatest, equals 20 percent or more of the principal amount of the secured class of securities.

PART 211—INTERPRETATIONS RELATING TO FINANCIAL REPORTING MATTERS

Subpart A—[Amended]

4. Part 211, subpart A, is amended by adding "Financial Statements and Periodic Reports For Related Issuers and Guarantors, Appendices A, B and C," Release No. FR-55 and the release date of August 4, 2000, to the list of interpretive releases.

Subpart B—[Amended]

5. Part 211 is amended by removing and reserving Staff Accounting Bulletin No. 53 to the table found in Subpart B.

PART 228—INTEGRATED DISCLOSURE SYSTEM FOR SMALL BUSINESS ISSUERS

6. The authority citation for part 228 continues to read as follows:

Authority: 15 U.S.C. 77e, 77f, 77g, 77h, 77j, 77k, 77s, 77z-2, 77aa(25), 77aa(26), 77ddd, 77eee, 77ggg, 77hhh, 77jjj, 77nnn, 77sss, 781, 78m, 78n, 78o, 78u-5, 78w, 7811, 80a-8, 80a-29, 80a-30, 80a-37, and 80b-11, unless otherwise noted.

7. Section 228.310 is amended by redesignating Note 3 as Note 5 and adding new Notes 3 and 4 to read as follows:

§ 228.310 (Item 310) Financial Statements.

Notes:

* * * * *

3. Financial statements for a subsidiary of a small business issuer that issues securities guaranteed by the small business issuer or guarantees securities issued by the small business issuer must be presented as required by Rule 3-10 of Regulation S-X (17 CFR 210.3-10), except that the periods presented are those required by paragraph (a) of this item.

4. Financial statements for a small business issuer's affiliates whose securities constitute

a substantial portion of the collateral for any class of securities registered or being registered must be presented as required by Rule 3-16 of Regulation S-X (17 CFR 210.3-16), except that the periods presented are those required by paragraph (a) of this item.

* * * * *

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

7. The authority citation for part 240 continues to read, in part, as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78f, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78o, 78p, 78q, 78s, 78u-5, 78w, 78x, 7811(d), 78mm, 79q, 79t, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4 and 80b-11, unless otherwise noted.

8. Section 240.12h-5 is added to read as follows:

§ 240.12h-5 Exemption for subsidiary issuers of guaranteed securities and subsidiary guarantors.

(a) Any issuer of a guaranteed security, or guarantor of a security, that is permitted to omit financial statements by § 210.3-10 of Regulation S-X of this chapter is exempt from the requirements of Section 13(a) or 15(d) of the Act (15 U.S.C. 78m(a) or 78o(d)).

(b) Any issuer of a guaranteed security, or guarantor of a security, that would be permitted to omit financial statements by § 210.3-10 of Regulation S-X of this chapter, but is required to file financial statements in accordance with the operation of § 210.3-10(g) of Regulation S-X of this chapter, is exempt from the requirements of Section 13(a) or 15(d) of the Act (15 U.S.C. 78m(a) or 78o(d)).

PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934

9. The authority citation for Part 249 continues to read, in part, as follows:

Authority: 15 U.S.C. 78a, *et seq.*, unless otherwise noted.

10. Effective September 30, 2000, amend Form 20-F (referenced in § 249.220f), first sentence of Instruction 1 of "Instructions to Item 8", by revising the phrase "3-10 and 3-14" to read "3-10, 3-14 and 3-16".

By the Commission.

Dated: August 4, 2000.

Margaret H. McFarland,
Deputy Secretary.

Note: Appendices A, B and C to the preamble will not appear in the Code of Federal Regulations.

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Appendix A—What does "100% owned" mean under Rule 3-10?
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Appendix A—What Does "100% Owned" Mean Under Rule 3-10?

Example No. 1: Parent company owns 100% of the voting shares of SubA. SubA owns 100% of the voting shares of Sub1.

Is SubA a 100%-owned subsidiary of the parent company? Yes.

Is Sub1 a 100%-owned subsidiary of SubA? Yes.

Is Sub1 an indirect, 100%-owned subsidiary of the parent company? Yes.

Example No. 2: Parent company owns 100% of the voting shares of SubA. SubA owns 99% of the voting shares of Sub1. The remaining 1% of the voting shares of Sub1 is owned by a party that is not a 100%-owned subsidiary of the parent company.

Is SubA a 100%-owned subsidiary of the parent company? Yes.

Is Sub1 a 100%-owned subsidiary of SubA? No.

Is Sub1 an indirect, 100%-owned subsidiary of the parent company? No.

Example No. 3: Parent company owns 99% of the voting shares of SubA. The remaining 1% of the voting shares of SubA are owned by a party that is not a 100%-owned subsidiary of the parent company. SubA owns 100% of the voting shares of Sub1.

Is SubA a 100%-owned subsidiary of the parent company? No.

Is Sub1 a 100%-owned subsidiary of SubA? Yes.

Is Sub1 an indirect, 100%-owned subsidiary of the parent company? No.

Example No. 4: Parent company owns 100% of the voting shares of SubA and 100% of the voting shares of SubB. SubA owns 60% of the voting shares of Sub1 and SubB owns 40% of the voting shares of Sub1.

Is SubA a 100%-owned subsidiary of the parent company? Yes.

Is SubB a 100%-owned subsidiary of the parent company? Yes.

Is Sub1 a 100%-owned subsidiary of SubA? No.

Is Sub1 a 100%-owned subsidiary of SubB? No.

Is Sub1 an indirect, 100%-owned subsidiary of the parent company? Yes.

Example No. 5: Parent company owns 100% of the voting shares of SubA. Parent company also owns 60% of the voting shares of Sub1. SubA owns 40% of the voting shares of Sub1.

Is SubA a 100%-owned subsidiary of the parent company? Yes.

Is Sub1 a 100%-owned subsidiary of SubA? No.

Is Sub1 an indirect, 100%-owned subsidiary of the parent company? Yes.

Example No. 6: Parent company owns 99% of the voting shares of SubA. As required by the law in its home country, a director of SubA owns the remaining 1% of the voting shares of SubA. SubA owns 100% of the voting shares of Sub1.

Is SubA a 100%-owned subsidiary of the parent company? No.

Is Sub1 a 100%-owned subsidiary of SubA? Yes.

Is Sub1 an indirect, 100%-owned subsidiary of the parent company? No.

Note: This situation is discussed in the release. Under these facts, you may wish to request a no-action letter from the Division of Corporation Finance.

Example No. 7: Parent company owns 100% of the voting shares of SubA. SubA has outstanding securities convertible into its voting shares. These convertible securities are held by a party that is not a 100%-owned subsidiary of the parent.

Is SubA a 100%-owned subsidiary of the parent company? No.

Example No. 8: Parent company owns 100% of the voting shares of SubA. SubA has outstanding securities convertible into the parent company's voting shares. These convertible securities are held by a party that is not a 100%-owned subsidiary of the parent.

Is SubA a 100%-owned subsidiary of the parent company? Yes.

Example No. 9: Parent company owns 100% of the voting shares of SubA. SubA has outstanding options exercisable into its voting shares. These options are held by a party that is not a 100%-owned subsidiary of the parent.

Is SubA a 100%-owned subsidiary of the parent company? No.

Example No. 10: Parent company owns 100% of the voting shares of SubA. SubA has outstanding options exercisable into the parent company's voting shares. These options are held by a party that is not a 100%-owned subsidiary of the parent.

Is SubA a 100%-owned subsidiary of the parent company? Yes.

Example No. 11: Parent company owns 100% of the common stock of SubA. SubA has a class of preferred stock outstanding.

That preferred stock is 100% owned by a party that is not a 100%-owned subsidiary of the parent company. The common equity has full voting rights. The preferred stock is non-voting.

Is SubA a 100%-owned subsidiary of the parent company? Yes.

Appendix B—Recently Acquired Subsidiary Issuers or Subsidiary Guarantors

The following examples illustrate the application of Rule 3-10(g) in determining the financial statements to be provided for recently acquired subsidiary issuers or subsidiary guarantors. For ease of use, we have included only subsidiary guarantor examples in this appendix. You should note, however, that Rule 3-10(g) applies equally to subsidiary issuers and subsidiary guarantors.

Each example is independent of the others. In each of the following examples, assume, unless stated otherwise, that:

- Parent company registers an offering of its debt securities under the Securities Act. The securities are guaranteed by one or more of its subsidiaries.
- Parent company and all acquired subsidiary guarantors have December 31

fiscal year ends and, unless otherwise specified, the parent company has filed its audited consolidated financial statements for the fiscal year in which the subsidiary was acquired.

- All subsidiaries are 100% owned.
- All guarantees are full and unconditional.
- All guarantees are joint and several.
- Each subsidiary's purchase price exceeds its net book value at its fiscal year end preceding the date of acquisition. The purchase price is used for testing significance.

This Appendix addresses only the requirements of Rule 3-10(g) of Regulation S-X. In each example, audited financial statements for additional periods may be required by Rule 3-05 of Regulation S-X.

Example No. 1: Significant acquired guarantor included more than nine months .

Subsidiary A was acquired on March 1, and has been included in its parent company's audited consolidated financial statements for ten months of the most recent fiscal year. Subsidiary A's purchase price exceeds 20% of the principal amount of the debt being registered.

Required financial information: No pre-acquisition financial statements of Subsidiary A are required. Although Subsidiary A's purchase price exceeds 20% of the principal amount of the debt being registered, financial statements may be omitted because Subsidiary A has been included in its parent company's audited consolidated financial statements for more than nine months of the most recent fiscal year.

Example No. 2: Significant acquired guarantor included less than nine months.

Subsidiary B was acquired on September 1, and has been included in its parent company's audited consolidated financial statements for four months of the most recent fiscal year. Subsidiary B's purchase price exceeds 20% of the principal amount of the debt being registered.

Required financial information: Pre-acquisition financial statements of Subsidiary B are required. Subsidiary B is significant and has been included in its parent company's audited consolidated financial statements for less than nine months of the most recent fiscal year. Audited financial statements of Subsidiary B for its most recent fiscal year preceding the acquisition and subsequent unaudited interim financial statements are required.

Example No. 3: Insignificant acquired guarantor. Subsidiary C was acquired on July 1, and has been included in its parent company's audited consolidated financial statements for six months of the most recent fiscal year. Subsidiary C's purchase price is less than 20% of the principal amount of the debt being registered.

Required financial information: Pre-acquisition financial statements of Subsidiary C are not required because Subsidiary C's purchase price is less than 20% of the principal amount of the debt being registered.

Example No. 4: Acquisition of significant business by pre-existing guarantor.

The assets and operations of Business D were acquired on October 1, and have been included in its parent company's audited

consolidated financial statements for three months of the most recent fiscal year. Upon acquisition, the assets and operations of Business D were transferred to pre-existing Subsidiary Guarantor X, which had little or no assets or operations. Business D's purchase price exceeds 20% of the principal amount of the debt being registered.

Required financial information: Pre-acquisition financial statements of Business D are required. Although Subsidiary Guarantor X has been included in the consolidated financial statements for more than nine months of the most recent fiscal year, Business D is considered a predecessor of Subsidiary Guarantor X. Audited financial statements of Business D for its most recent fiscal year preceding the acquisition and subsequent unaudited interim financial statements are required.

Example No. 5: Acquisition of multiple related guarantors.

Subsidiaries E and F were acquired on August 1, and have been included in their parent company's audited consolidated financial statements for five months of the most recent fiscal year. Consummation of each acquisition was conditioned upon the other.

Subsidiary E and F's purchase prices were 12% and 17% of the principal amount of the debt being registered, respectively.

Required financial information: Pre-acquisition financial statements of Subsidiaries E and F are required. Because the acquisitions are related, their individual significance levels must be aggregated. Their aggregate purchase price exceeds 20% of the principal amount of the debt being registered. If Subsidiaries E and F were under common control or management before their acquisition, combined financial statements may be presented. Otherwise, separate financial statements are required. Audited financial statements of Subsidiaries E and F for their most recent fiscal years preceding the acquisition and subsequent unaudited interim financial statements are required.

Example No. 6: Acquisition of multiple unrelated guarantors.

Subsidiary G was acquired on May 1, and Subsidiary H was acquired on June 1. Subsidiaries G and H have been included in their parent company's audited consolidated financial statements for eight and seven months of the most recent fiscal year, respectively. The acquisitions are not related by common ownership, common management, or common conditions to consummation. Subsidiary G and H's purchase prices were 11% and 18% of the principal amount of the debt being registered, respectively.

Required financial information: Pre-acquisition financial statements of Subsidiaries G and H are not required. Because the acquisitions are unrelated, their significance levels are assessed individually. Each subsidiary is less than 20% of the principal amount of the debt being registered.

Example No. 7: Very Recent Acquisition of Significant Guarantor.

Subsidiary I was acquired on April 1, after the end of the parent company's most recent fiscal year. Subsidiary I is not yet included in the parent company's audited

consolidated financial statements. Subsidiary I's purchase price exceeds 20% of the principal amount of the debt being registered. Parent Company files a Securities Act registration statement on April 2.

Required Financial Information: Pre-acquisition financial statements of Subsidiary I are required. Subsidiary I is significant and has not been included in its parent company's consolidated financial statements for nine months of the most recent fiscal year. Audited financial statements of Subsidiary I for its most recent fiscal year preceding the acquisition are required. The 75 day post-consummation period generally available to a recently acquired business under Rule 3-05 is not applicable to Rule 3-10(g).

Example No. 8: Acquisition of Significant Guarantor Not Yet Consummated.

Parent company contemplates the acquisition of Business J. If acquired, Business J will become a subsidiary guarantor of the debt securities being registered. Consummation has not occurred at the time of effectiveness of the registration statement. Business J's purchase price would exceed 20% of the principal amount of the debt being registered.

Required Financial Information: Pre-acquisition financial statements of Business J are not required under Rule 3-10(g). Business J is not a guarantor at the time of effectiveness of the registration statement. However, as for all businesses to be acquired, the parent company must separately evaluate whether pre-acquisition financial statements of Business J are required by Rule 3-05.

Example No. 9: Significant Guarantor in a Pooling of Interests.

Subsidiary K became a subsidiary on December 1 in a pooling of interests transaction. As a result of application of the pooling of interests method, Subsidiary K is included retroactively in its parent company's audited consolidated financial statements for all three years. Subsidiary K's net book value exceeds 20% of the principal amount of the debt being registered.

Required Financial Information: Pre-acquisition financial statements of Subsidiary K are not required. Inclusion of Subsidiary K in its parent company's condensed consolidating financial information under Rule 3-10 for all periods presented satisfies the requirements of Rule 3-10(g).

Appendix C—Who Is the “Parent Company” Under Rule 3-10?

Example No. 1:

- Company A is an Exchange Act reporting company.
- Company A owns 100% of Company B.
- Company B is not an Exchange Act reporting company.
- Company B issues securities.
- Company A guarantees those securities.
- No other company in this corporate structure co-issues or guarantees the securities.

Company A is the “parent company” for purposes of applying Rule 3-10 to the subject securities.

Example No. 2:

- Company A is an Exchange Act reporting company.

- Company A issues securities.
- Company A owns 100% of Company B.
- Company B is not an Exchange Act reporting company.

• Company B guarantees the subject securities.

• No other company in this corporate structure co-issues or guarantees the securities.

Company A is the “parent company” for purposes of applying Rule 3–10 to the subject securities.

Example No. 3:

• Company A is an Exchange Act reporting company.

• Company A owns 100% of Company B.

• Company B is an Exchange Act reporting company.

• Company B issues securities.

• Company B owns 100% of Company C.

• Company C is not an Exchange Act reporting company.

• Company C guarantees the subject securities.

• Neither Company A nor any other company in this corporate structure co-issues or guarantees the securities.

Company B is the “parent company” for purposes of applying Rule 3–10 to the subject securities. The consolidated financial statements of Company A may not be substituted for those of Company B, even if Company A’s financial statements are substantially the same as Company B’s. The parent company for purposes of Rule 3–10 must be an issuer or guarantor of the subject security.

Example No. 4:

• Company A is not an Exchange Act reporting company.

• Company A owns 100% of Company B.

• Company B is an Exchange Act reporting company.

• Company B issues securities.

• Company B owns 100% of Company C.

• Company C is not an Exchange Act reporting company.

• Company C guarantees the subject securities.

• Neither Company A nor any other company in this corporate structure co-issues or guarantees the securities.

Company B is the “parent company” for purposes of applying Rule 3–10 to the subject securities.

Example No. 5:

• Company A is an Exchange Act reporting company.

• Company A owns 100% of Company B.

• Company B is an Exchange Act reporting company.

• Company B owns 100% of Company C.

• Company C is not an Exchange Act reporting company.

• Company C issues securities.

• Company A and Company B guarantee the subject securities.

• No other company in this corporate structure co-issues or guarantees the securities.

Company A is the “parent company” for purposes of applying Rule 3–10 to the subject securities. The consolidated financial statements of Company B may not be substituted for those of Company A, even if Company B’s financial statements are substantially the same as Company A’s. There are no exceptions to the parent company’s obligation to provide the financial statements for a registrant under Rule 3–10(a).

Example No. 6:

• Company A is an Exchange Act reporting company.

• Company A owns 100% of Company B and Company C.

• Neither Company B nor Company C is an Exchange Act reporting company.

• Company B owns 50% of Company D.

• Company C owns the other 50% of Company D.

• Company D is not an Exchange Act reporting company.

• Company D owns 100% of Company E.

• Company E is not an Exchange Act reporting company.

• Company E issues securities.

• Companies A, B, C, and D guarantee the subject securities.

• No other company in this corporate structure co-issues or guarantees the securities.

Company A is the “parent company” for purposes of applying Rule 3–10 to the subject securities.

Example No. 7:

• Company A is not Exchange Act reporting company.

• Company A owns 100% of Company B and Company C.

• Neither Company B nor Company C is an Exchange Act reporting company.

• Company B owns 50% of Company D.

• Company C owns the other 50% of Company D.

• Company D is an Exchange Act reporting company.

• Company D owns 100% of Company E.

• Company E is not an Exchange Act reporting company.

• Company E issues securities.

• Company D guarantees the subject securities.

• No other company in this corporate structure co-issues or guarantees the securities.

Company D is the “parent company” for purposes of applying Rule 3–10 to the subject securities.

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