

SEC Proposes Changes to Facilitate Registered Guaranteed and Secured Debt Offerings

July 31, 2018

On July 24, 2018, the SEC announced proposed amendments (the “Proposal”) to streamline the financial disclosure requirements of Rule 3-10 of Regulation S-X for guarantors and issuers of registered guaranteed debt securities and the financial disclosure requirements of Rule 3-16 of Regulation S-X for affiliates whose securities collateralize registered secured debt securities. As a result of existing eligibility restrictions and disclosure obligations, most guaranteed or secured debt offerings today are either not registered with the SEC or, if registered, are structured to avoid triggering more extensive financial disclosure under the existing rules.

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Registered guaranteed debt securities under Rule 3-10: The Proposal would amend existing Rule 3-10 as follows:

- *Ownership threshold:* Under the Proposal, a subsidiary issuer or guarantor would no longer need to be 100 percent owned by the parent company to qualify under the rule. Instead, the proposed rule would require only that the subsidiary issuer or guarantor be consolidated in the parent company's consolidated financial statements.
- *Substance of disclosure:* Under existing Rule 3-10, a parent company must provide detailed condensed consolidating financial information of the subsidiary issuer or guarantor covering the same periods as the parent's consolidated financial statements. The Proposal would replace this with a requirement to provide summarized financial information (as defined in Rule 1-02(bb)(1) of Regulation S-X). It would also expand the qualitative disclosure about the guarantees and the issuers and guarantors, including disclosure of additional information that would be material to holders of the guaranteed securities. Finally, the Proposal would reduce the number of periods required to be covered and would eliminate the requirement to provide pre-acquisition financial statements of recently acquired subsidiary issuers and guarantors.
- *Placement of disclosure:* Rule 3-10 requires the applicable disclosure to be included in the footnotes to the parent company's consolidated financial statements. Under the Proposal, the proposed required disclosure could be provided outside the footnotes to the parent's financial statements in a registration statement covering the subject securities and any related prospectus (as well as certain Exchange Act reports filed shortly thereafter). The proposed required disclosure would, nonetheless, be required

in the parent's financial statements for annual and quarterly reports beginning with the annual report for the fiscal year during which the first bona fide sale of the subject securities is completed.

- *Duration of disclosure obligation:* Currently, the obligation to provide disclosure under Rule 3-10 survives for as long as the guaranteed securities are outstanding. The Proposal would limit the duration of the obligation to only as long as the issuers and guarantors have an Exchange Act reporting obligation with respect to such securities.

Registered secured debt securities under Rule 3-16: The Proposal would amend existing Rule 3-16 as follows:

- *Substance of disclosure:* Existing Rule 3-16 requires a registrant to provide separate financial statements for each affiliate whose securities are pledged and constitute a "substantial portion" of the collateral for a class of registered securities. Under the Proposal, the registrant will only be required to provide financial and non-financial disclosures as a supplement to the registrant's consolidated financial statements.
- *Quantitative threshold:* Presently, the disclosure requirements of Rule 3-16 apply when the pledged securities meet or exceed a quantitative threshold relative to the amount of registered securities under the "substantial portion" test. The Proposal would replace this test with a requirement to provide the proposed financial and non-financial disclosure only to the extent it would be material to holders of the collateralized securities.
- *Placement of disclosure:* Under existing Rule 3-16, the registrant includes the affiliate financial statements together with its own financial statements. The proposed financial and non-financial disclosures under Rule 3-16 would be permitted to be located in filings in the same manner described above for disclosures related to guarantors and guaranteed securities.

We welcome you to reach out to us with any questions or if you or your organization are interested in commenting on the Proposal.

Peter J. Loughran
Partner, New York
+1 212 909 6375
pjloughran@debevoise.com

Matthew E. Kaplan
Partner, New York
+1 212 909 7334
mekaplan@debevoise.com

Paul M. Rodel
Partner, New York
+1 212 909 6478
pmrodel@debevoise.com

Steven J. Slutzky
Partner, New York
+1 212 909 6036
sjslutzky@debevoise.com

Lauren M. Isaacson
Associate, New York
+1 212 909 6106
lisaacson@debevoise.com

Trey Reilly
Associate, New York
+1 212 909 6678
treilly@debevoise.com