



SEC Proposes Amendments to Financial Disclosure Rules for Guaranteed and Secured Debt Securities

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Rule 3-10: Guaranteed Debt Securities

Current Requirements

A guarantee of a debt security is a separate security under the Securities Act, and therefore offers and sales of such guarantees must be either registered or exempt from registration under the Securities Act. In a registered offering of guaranteed securities, each guarantor is viewed as an issuer and required to provide separate financial statements, subject to exceptions in Rule 3-10 for full and unconditional guarantees in corporate structures in which each guarantor or issuer subsidiary is 100 percent owned by its parent entity. If the Rule's detailed conditions are met, specified "Alternative Disclosures" may be provided under Rule 3-10 in lieu of separate financial statements for each issuer and guarantor.

Proposed Amendments

The proposed amendments to Rule 3-10 would continue to permit the omission of separate financial statements of subsidiary issuers and guarantors subject to certain conditions, which would also be simplified by the proposed amendments. If the conditions are met, an issuer may present "Proposed Alternative Disclosures" that generally simplify the required disclosures compared to the existing rules. In particular, the proposed amendments would:

- replace the condition that a subsidiary issuer or guarantor be 100 percent owned by the parent company with a condition that it be consolidated in the parent company's consolidated financial statements

- replace the requirement to present detailed, condensed, consolidating financial information in many situations with a requirement to present summarized financial information, as defined in Rule 1-02 of Regulation S-X, which may be presented on a combined basis for the most recent fiscal year and interim period
- expand the required non-financial disclosures, including qualitative narrative disclosures about the guarantees, issuers and guarantors
- permit the Proposed Alternative Disclosures to be provided outside the footnotes to the parent company's consolidated financial statements in the registration statement covering the offer and sale of the subject securities and in certain Exchange Act reports filed shortly thereafter, which is intended to facilitate offerings during favorable market conditions without the cost and delay of preparing audited financial information under the existing rules
- require that the Proposed Alternative Disclosures be included in the footnotes to the parent company's consolidated financial statements beginning with the annual report for the fiscal year during which the first bona fide sale of the subject securities is completed
- eliminate the requirement to provide detailed pre-acquisition financial statements of recently-acquired subsidiary issuers and guarantors under Rule 3-10(g)
- simplify the eligibility criteria for issuer and guarantor parent and subsidiary structures
- permit the Proposed Alternative Disclosures to be terminated if the issuers and guarantors can terminate or suspend their Exchange Act reporting obligations with respect to the guaranteed securities, rather than continuing to require the supplemental disclosures for as long as the guaranteed securities are outstanding.

Rule 3-16: Affiliates Whose Securities Collateralize a Registrant's Securities

Current Requirements

Rule 3-16 requires a registrant to provide separate financial statements for each affiliate whose securities constitute a "substantial portion" of the collateral for any class of registered securities. Whether an affiliate's portion of the collateral is a "substantial portion" is determined by comparing the principal amount of the registered securities to the highest amount among the aggregate principal amount, par value, book value, or market value of the affiliate's securities. If the highest of those values equals or exceeds 20% of the principal amount of the registered securities, separate financial statements are required.

Proposed Amendments

The proposed amendments to Rule 3-16 would simplify the disclosures required for affiliates whose securities collateralize registered securities and provide for more consistent presentation by removing the existing 20 percent threshold. Among other things, the amendments would:

- replace the existing requirement to provide separate financial statements for each affiliate whose securities are pledged as collateral with specified supplemental financial and non-financial disclosures about the affiliate(s) and the collateral arrangement, which may be presented on a combined basis, subject to certain conditions
- permit the proposed supplemental financial and non-financial disclosures to be provided outside the footnotes to the registrant's consolidated financial statements in the registration statement covering the offer and sale of the subject securities, and in certain Exchange Act reports filed shortly thereafter, to facilitate offerings during favorable market conditions
- require that the proposed supplemental financial and non-financial disclosures be included in the footnotes to the registrant's consolidated financial statements beginning with the annual report for the fiscal year during which the first bona fide sale of the subject securities is completed
- replace the requirement to provide disclosure only when the pledged securities meet or exceed a numerical threshold (the 20 percent test) relative to the registered securities with a requirement to provide the proposed financial and non-financial disclosures in all cases, unless they are immaterial to holders of the collateralized security.

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