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

Re: File Number S7-05-19

RSM US LLP appreciates the opportunity to offer our comments on SEC Release No. 33-10635, *Amendments to Financial Disclosures about Acquired and Disposed Businesses* (the proposed rule). RSM US LLP is a registered public accounting firm serving middle-market issuers, brokers and dealers.

We appreciate the Commission's efforts to review the Regulation S-X requirements applicable to financial disclosures about acquired and disposed businesses. We support the overarching objective of the proposed rule "to improve for investors the financial information about acquired or disposed businesses, facilitate more timely access to capital, and reduce the complexity and costs to prepare the disclosure."

We generally support the provisions of the proposed rule, and have provided comments that address potential challenges in applying some of the proposed rules in practice. Our views expressed in this letter are based on our experience in working with registrants as well as private companies whose financial statements are required to be included in filings with the SEC.

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

The investment, asset and income significance tests defined in S-X Rule 1-02(w) are used in various SEC rules and regulations to determine whether financial statements of entities other than the registrant, such as acquired companies under S-X Rule 3-05 and equity-method investees under S-X Rule 3-09, must be included in SEC filings.

Investment test under proposed S-X Rule 1-02(w)(1)(i)

With respect to the investment test in proposed Rule 1-02(w)(1)(i), which would compare the registrant's and its other subsidiaries' investments in and advances to the tested subsidiary with the aggregate worldwide market value of the registrant's voting and non-voting common equity, we have the following comments:

- Instead of determining the aggregate worldwide market value of the registrant's voting and non-voting common equity as of the last business day of the registrant's most recently completed fiscal year, we recommend aligning this measurement date with the last business day of the registrant's most recently completed fiscal quarter prior to the public announcement of the transaction. We believe a more current date would result in a more meaningful test because the worldwide market value of the registrant could change significantly after the last business day of the registrant's most recently completed fiscal year.
- In an initial public offering, we recommend allowing a company to estimate its worldwide market value at the anticipated offering date.

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

The income test in proposed Rule 1-02(w)(1)(iii)(A)(1) would compare the absolute value of the registrant's and its other subsidiaries' equity in the tested subsidiary's consolidated income or loss from continuing operations (after intercompany eliminations) attributable to the controlling interests with the absolute value of such income or loss of the registrant and its subsidiaries consolidated for the most recently completed fiscal year. We believe the use of after-tax income for this test may result in inconsistent determinations due to, for example, the unrelated volatility in income taxes (e.g., tax law changes) and the fact that a pass-through entity could appear to be more significant to the registrant than a tax-paying entity. We recommend that the income test continue to be based on pretax income or pretax income prior to interest as the cost capitalization of the entity may not be meaningful to the results.

The income test in proposed Rule 1-02(w)(1)(iii)(A)(2) would compare the registrant's and its other subsidiaries' proportionate share of the tested subsidiary's' consolidated total revenue with such total revenue of the registrant and its subsidiaries consolidated for the most recently completed fiscal year. However, this component does not apply if either the registrant and its subsidiaries consolidated or the tested subsidiary does not have "recurring annual revenue." To ensure consistent application of this rule, we suggest the Commission define "recurring annual revenue."

Investment company considerations

In the income test of proposed Rule 1-02(w)(2)(ii) for a registrant that is a registered investment company or a business development company, we suggest the Commission clarify whether the numerator for the tested subsidiary should be calculated as (a) the absolute value of the sum of investment income from dividends, interest and other income, the net realized gains and losses on investments, and the net change in unrealized gains and losses on investments, or (b) the sum of the individual absolute values of each of these components.

Also, proposed Rule 1-02(w)(2)(ii)(B) states, "However, if the registrant and its subsidiaries consolidated has an insignificant change in net assets resulting from operations for its most recently completed fiscal year, compute the test using the average of the absolute value of such amounts for the registrant and its subsidiaries consolidated for each of its last five fiscal years." To avoid inconsistency in the application of this provision, we suggest the Commission consider defining "insignificant change."

Five-year income averaging

Five-year income averaging is included in the alternate income test in proposed rule 1-02(w)(2)(ii)(B), but is not included in the 80 percent income test in proposed rule 1-02(w)(2)(ii)(A). Since this presents a discrepancy in permitting the use of five-year income averaging, we recommend the Commission clarify whether an investment company is permitted to use five-year income averaging in the 80 percent income test in proposed rule 1-02(w)(2)(ii)(A).

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

Independence

Proposed Rule 3-05(a) (and proposed Rules 3-14(a) and 6-11) requires financial statements to be prepared and audited in accordance with Regulation S-X (including the independence standards in Rule 2-01 "or, alternatively, if the business is not a registrant, the applicable independence standards"). To avoid confusion, we suggest the final rules clarify that the independence standards to be applied should be those related to the auditing standards under which the required financial statements of the acquired or to-be-acquired business were audited.

Individually insignificant businesses

Similar to existing requirements, proposed Rule 3-05(b)(2)(iv) would require disclosure of the aggregate impact of businesses acquired or to be acquired since the date of the most recent audited balance sheet filed for the registrant, for which financial statements are either not required by paragraph (b)(2)(i) or are not yet required based on paragraph (b)(4)(i), exceeds 50%. The proposed rule, however, would require registrants to provide pro forma financial information depicting the aggregate impact of all such businesses in all material respects and pre-acquisition historical financial statements only for those businesses whose individual significance exceeds 20% but are not yet required to file financial statements. This proposed rule change could have three potential implications that we wish to bring to your attention:

- Underwriters may request that the underlying information for insignificant acquisitions be audited or reviewed, which could impose additional cost and time burdens on the registrant
- When the registrant includes the effects of individually insignificant acquisitions for which historical financial statements have not been audited or reviewed, without a change in current auditing standards, the accountant will not be able to provide negative assurance on the combined pro forma information required by proposed Rule 3-05(b)(2)(iv)(A) because Public Company Accounting Oversight Board (PCAOB) Auditing Standard (AS) 6101, *Letters for Underwriters and Certain Other Requesting Parties*, prohibits accountants from providing negative assurance on pro forma financial information if the underlying historical periods are not audited or reviewed.
- Registrants could have different interpretations of what it means to provide pro forma financial information that depicts the aggregate impact of acquired or to be acquired businesses in *all material respects* (emphasis added). We recommend the Commission consider defining "all material respects" or discussing examples that do not depict the aggregate impact in all material respects.

Financial statements of a foreign business

The requirements for financial statements of a foreign business in proposed Rule 3-05(c) are different than those in proposed Rule 3-05(d) that are applicable to a business that would be a foreign private issuer if it were a registrant. Having two different rules for essentially the same entities, which result in different financial statement requirements, can cause confusion and inconstancy in information provided. We recommend the Commission consider eliminating proposed Rule 3-05(d) and making the requirements in proposed Rule 3-05(c) also be applicable to a business that would be a foreign private issuer if it were a registrant.

Use of abbreviated financial statements

We have encountered situations in which our clients could not comply, or had difficulty complying, with the provisions of S-X Rule 3-05 because it was impracticable to prepare the full financial statements for all required periods. We believe the proposed rule will reduce complexity and financial reporting burdens because it encompasses the SEC staff's current approach for evaluating requests to provide audited abbreviated financial statements (i.e., statements of revenue and direct expenses and statements of assets acquired and liabilities assumed) when complete financial statements are not obtainable or readily available. We believe additional clarity could be provided by:

- Defining the following terms used in proposed Rule 3-05(e)(1): *separate entity, subsidiary, segment* and *division.*

- Addressing the appropriateness of providing carve-out financial statements, which are discussed in Section 2065.3 of the Division of Corporation Finance *Financial Reporting Manual*, but are not discussed in the proposed rule.

Omission of Rule 3-05 pre-acquisition financial statement of an acquired business

In connection with initial registration statements, the proposed rule would allow a registrant to omit pre-acquisition financial statements for acquisitions that have been included in its post-acquisition audited results for at least a “complete fiscal year.” However, currently, an IPO candidate can omit pre-acquisition financial statements of an acquired business that is at least 20%, but not more than 40%, significant, if the business has been included in its post-acquisition audited results for at least nine months. We recommend the Commission consider allowing IPO candidates to continue to omit pre-acquisition financial statements of an acquired business in these circumstances.

Blind pool offerings

The Commission has proposed new Rule 3-14(b)(2)(iii) to codify current staff interpretations regarding the computation of significance for blind pool real estate offerings. We suggest the Commission consider extending this accommodation to all blind pool offerings within the scope of Rule 3-05.

Proposed S-X Rule 3-14, *Special instructions for financial statements of real estate operations acquired or to be acquired*

Proposed Rule 3-14(c)(2)(iii) requires disclosure in the notes to the financial statements of information about a real estate operation’s “operating, investing and financing cash flows, to the extent available.” Such historical investing and financing cash flow information may not be comparable to proposed future operations. Therefore it is unclear why disclosure of this cash flow information would be required since Rule 3-14 financial statements consist only of statements of revenues and expenses, which exclude expenses not comparable to proposed future operations.

Proposed Article 11 – *Pro Forma Financial Information*

Management’s Adjustments

Proposed Rule 11-02(a)(6)(ii) introduces the concept of “Management’s Adjustments” – adjustments that give effect to reasonably estimable synergies and other transaction effects. Because this broad definition may cause inconsistencies in application, we suggest the Commission provide supplementary guidance regarding Management’s Adjustments to address implementation questions, such as:

- Are there additional examples of “synergies and other transaction effects”?
- Is there a time limit by when the synergies and other transaction effects should be expected to occur (e.g., within x months of the transaction)?
- What criteria need to be met for the synergies and other transaction effects to be “reasonably estimable”?
- What qualitative information is necessary to give a fair and balanced presentation of the pro forma information as required by proposed Rule 11-02(a)(10)(iii)?

Also, given the subjectivity involved in determining Management’s Adjustments, the Commission should consider inquiring with the PCAOB regarding the effects of the proposed rule on the auditor’s ability to provide negative assurance in a comfort letter on (a) the application of pro forma adjustments to historical

amounts in the compilation of pro forma financial information and (b) whether the pro forma financial information complies as to form in all material respects with the applicable accounting requirements of Rule 11-02.

Consistency with U.S. GAAP

To the extent Topic 805, "Business Combinations," of the Financial Accounting Standards Board (FASB) Accounting Standards Codification is silent as to specific requirements, registrants preparing pro forma financial information under ASC 805 often analogize to the requirements in Article 11. There is currently disparity in disclosure between the GAAP financials statements and the pro forma disclosures. If the FASB concludes that the proposed changes to Article 11 do not impact the pro forma information provided in accordance with ASC 805, more disparity between SEC and FASB requirements could occur. Therefore, we recommend the Commission dialogue with the FASB regarding the implications of the proposed changes to Article 11.

Scaled disclosures for smaller entities

We believe the investing community is in the best position to determine the appropriate extent of scaled disclosure provisions that provide the information necessary for capital formation. We also believe a single set of rules related to Rule 3-05, Rule 3-14 and Article 11, with scaled disclosure provisions, would create consistency across all entities with respect to the type of information provided. However, as explained in the following paragraphs, there may be unnecessary overlap and complexity in filer status definitions that causes confusion among smaller entities as to scaled disclosure and other requirements.

A "smaller reporting company" generally is a registrant with (a) less than $250 million in common equity public float as of the last business day of the company's most recently completed second fiscal quarter, or (b) annual revenues of less than $100 million in the most recently completed fiscal year and either no public float or a public float of less than $700 million. Therefore, a smaller reporting company can be a non-accelerated filer or an accelerated filer. The smaller reporting company qualification relates to scaled disclosure and not filing status. Because the current definitions of *smaller reporting company* and *non-accelerated filer* overlap for some issuers, there can be confusion.

Further, the current structure consisting of Regulation A issuers, emerging growth companies, smaller reporting companies, nonaccelerated filers, accelerated filers and large accelerated filers has led to a labyrinth of rules, which result in the smaller entities with the fewest resources putting in more effort, relative to size, in sorting through and complying with the rules.

We encourage the SEC to consider (a) defining the following terms using parameters that do not cause unnecessary overlap of the definitions and (b) including such definitions in one rule that provides scalability for all financial reporting regulations (e.g., scaled disclosures, filing deadlines, compliance with Section 404(b)):

- Regulation A issuers
- Emerging growth companies
- Smaller reporting companies
- Nonaccelerated filers
- Accelerated filers
- Large accelerated filers

Division of Corporation Finance *Financial Reporting Manual*

We recommend the Commission staff review all guidance in the Division of Corporation Finance *Financial Reporting Manual* that is related to the proposed rule to determine whether existing staff guidance should continue to apply, be revised or be eliminated.

We would be pleased to respond to any questions the Commission or its staff may have about our comments. Please direct any questions to Rich Davisson - Partner, National Professional Standards Group, at [redacted].

Sincerely,

RSM US LLP

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