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July 29, 2019

Via E-mail: rule-comments@sec.gov

Securities and Exchange Commission,
100 F Street, N.E.,
Washington, DC 20549-1090.

Attention: Vanessa Countryman, Secretary

Re: Amendments to Financial Disclosures about Acquired and Disposed Businesses -- File No.S7-05-19

Ladies and Gentlemen:

We appreciate the opportunity to present our views on the Commission's proposed amendments to its rules and forms addressing the disclosure requirements for financial information relating to acquisitions and dispositions of businesses.[1] We commend the Commission's efforts to focus these disclosures on material information and reduce the costs and burdens imposed on registrants, and support most of the proposed amendments, subject only to the few suggestions for improvement noted below. The one major aspect with which we do not agree is the proposed requirement to include, in pro forma financial information, a set of "Management's Adjustments" relating to

[1] Release No. 33-10635; 34-85765; IC-33465 (May 3, 2019) (the "Release").

synergies. For a variety of reasons explained below, while we think the Commission could reasonably require acquirors to make additional disclosures relating to expected synergies, we also feel strongly that this should not be implemented by means of required pro forma adjustments, and that the proposed Management's Adjustments requirement should therefore be dropped.

"Management's Adjustments" for Synergies in Pro Forma Financial Information

The proposed rules would require that pro forma financial information include "Management's Adjustments" constituting reasonably estimable synergies and other transaction effects that have occurred or are reasonably likely to occur. The Release indicates that this proposed change is intended to yield more useful information to investors, and to enable investors to hold boards and management more accountable for the synergy estimates they disclose. Rather than adding this Management's Adjustments requirement, we suggest that the Commission instead consider requiring narrative disclosure of synergies information in transactions in which such information has otherwise been publicly disclosed. If done properly, this would allow acquirors to share their perspective on expected synergies, placed in appropriate context, and would permit a more nuanced, and frankly more accurate, presentation than the "single point estimates" that would necessarily have to be reflected in any Management's Adjustments in pro forma financial information. Given the challenges and uncertainties involved in producing any synergies information, we think it would be essential that the Commission develop a principles-based, rather than an overly prescriptive, approach to any such

requirement. And given the complexity of this topic, we suggest that any such new disclosure requirement be reproposed and subjected to a new round of comments. But we do believe that acquirors that otherwise publicly disclose synergies information could reasonably be required, in a principles-based manner, to address the topic of synergies in their SEC filings.

Requiring a set of Management's Adjustments relating to synergies in Article 11 pro forma financial information is a very different proposition. In principle, if there was a straightforward and uniform measure of expected synergies, developed on the basis of generally accepted principles and prepared and presented in a consistent manner by all registrants, then requiring registrants to reflect that measure in their pro forma financial statements might well result in useful information being conveyed to investors. The problem is that no such generally accepted measure of synergies exists. Rather, synergies information is highly idiosyncratic, reflecting the particular circumstances of each transaction, and developed in different ways and for different purposes across transactions. Even setting aside comparability concerns, requiring that such adjustments be included in all pro forma financial statements would in many cases convey a false sense of precision, and thus be affirmatively misleading to investors. Specific issues with the proposed approach include the following:

1. The significance of anticipated synergies varies widely across acquisition transactions, very important in some cases but of little or no importance in others. The degree of uncertainty associated with synergy estimates similarly varies widely. And there are different kinds of synergies – cost

synergies (which we assume are the intended focus of the proposed requirement, but this would need to be clarified), as well as revenue synergies and capital synergies, which are commonly more difficult to estimate, less certain, and sometimes potentially sensitive for antitrust or other reasons. Whether and how to disclose such synergies information therefore requires fine judgment. There are many reasons why an acquiror might determine not to disclose, or to limit its disclosure of, synergies it actually expects to realize, including its level of confidence in the accuracy and attainability of the forecasted information, and its views as to materiality of the information, but also possible concerns about the impact such disclosure (or inferences drawn from it) might have on employee retention and morale, or on customer, vendor or landlord relationships. We therefore think an acquiror should definitely not be required to reflect pro forma adjustments for quantitative synergies information unless that information is otherwise being publicly disclosed. But even where the acquiror has made other synergies disclosure, reducing that disclosure to a single set of "Management's Adjustments" will be highly problematic, for a number of reasons.

2. One problem relates to variations in the expected timing of realization. Total synergies are often planned to be realized over several years, but the number of years can vary widely. And there is the related question as to timing of costs incurred to realize synergies, which may vary considerably

from the timing of related benefits. For example, the costs may be front end-loaded, relative to the benefits. The proposing release does not explain what portion of expected synergies, or which periods' synergy amounts, should be included as Management's Adjustments in the pro forma statements, or even how an acquiror should approach these questions.

3. Preparation of synergies information can be very challenging, since it is forward-looking and commonly needs to take into account information about operations not within the acquiror's control. Reducing the information so developed to a single set of "Management's Adjustments", in addition to being practically and conceptually very challenging, will also generally force issuers to recast this information for a new and unintended use. Multi-year synergies information is commonly intended to be layered onto multi-year forward-looking financial models, of the sort prepared by research analysts, and that will generally be its best and highest use. Information in respect of future periods is inherently uncertain, and the further into the future one projects, the greater the uncertainty. In the context of multi-year financial models, these relationships are intuitively clear. On the other hand, forcing such synergies information to be compressed into a single set of Managements' Adjustments, to be applied on a pro forma basis to combined *historical* results, simply does not reflect the way managements or boards or

shareholders think about potential synergies, and would therefore represent a sterile exercise. In addition to being very challenging, the "point estimate" nature of the presentation is also likely to suggest a false precision in the pro forma financial information, and thus to be inherently misleading.

4. The Commission should also consider that "reasonably estimable" may not correspond to the acquiror's or the target's decisional process, which may instead be based on ranges and relative probabilities. As a result, for this additional reason, Management's Adjustments may not in fact fairly reflect the perspective of the acquiror's management, in respect of the acquisition and its consequences.

5. Another problem we foresee relates to the fact that in many cases an acquiror will need to provide pro forma financial information at several different points in the acquisition process – for example, in a Form S-4/proxy statement seeking approval of the transaction, and in the Form 8-K filing due 75 days after closing, but often at additional times in connection with other financing transactions to fund the acquisition or that are simply contemporaneous with it. The acquiror's ability to develop the required Management's Adjustments will in most cases improve notably over that timeline, and so the reported Management's Adjustments can be expected to change as the transaction progresses and the acquiror discloses updated pro forma financial information. Due to the "false precision"

problem noted above, we fear that such changes in successively disclosed Management's Adjustments will attract undue attention and serve as a major distraction, if not an outright impediment, to completing transactions in a timely and efficient manner.

6. There are many practical considerations that would affect an acquiror's ability to develop the required Management's Adjustments, and thus the quality and reliability of that information. As noted above, the timing of the calculation will have a key effect, and so concerns as to quality and reliability are likely to be most troublesome in the context of proxy statement disclosure in respect of proposed acquisitions, given the potentially limited information as to the acquired company available to the acquiror at that early stage, and the frequently incomplete and preliminary nature of that information. The particular circumstances of a transaction may have a further unhelpful impact on the acquiror's ability to produce good estimates – for example, the practice in some situations, typically involving regulatory overlaps, to employ prophylactic "clean-team" procedures to permit due diligence to proceed, but without full sharing within the acquiror's organization of the results of that work.

7. We can also foresee a number of practical challenges that could arise, relative to other transaction elements, as a result of this new requirement to develop Management's Adjustments information, which will in effect be a different, and potentially competing, articulation of management's

synergies expectations. For example, how will the required Management's Adjustments relate to, or affect, the acquiror's own management projections provided to its board and shareholders, or the projections provided to financial advisors for purposes of rendering fairness opinions? And how might this newly-required information figure in appraisal litigation, where courts have recently show an interest in factoring synergies information into their analysis?

8. Further complications would arise in the context of transactions with a cross-border element, or involving U.S. registrants that are also subject to foreign reporting and disclosure requirements as a result of being listed (or having affiliates listed) outside of the United States. Some jurisdictions already regulate the publication of synergies estimates and projections in ways that differ significantly from the Management's Adjustments proposal. For example, in the context of a proposed acquisition of a company regulated by the Takeover Code of the United Kingdom, if an offeror makes a statement quantifying any financial benefits expected to accrue from a successful acquisition, then a report thereon is required from both the offeror's reporting accountants and its financial adviser. In part due to the prescriptive nature of the relevant U.K. rules and in part due to market practice of the accountants and advisers, these statements generally follow a standard format which would be challenging to align with the proposed Management's Adjustments formulation. The potential

application of Regulation M-A Item 1015(b) to such accountants' and advisers' reports already represents a significant challenge for U.S. offerors in such transactions, and the new Management's Adjustments requirements would just add to that problem.

Other Comments

As noted above, we support the proposed amendments (other than Management's Adjustments requirement), subject to the suggestions set out below. In particular, we support the changes limiting Rule 3-05 financial statements to the most recent two years; permitting the use of abbreviated financial statements where the business acquired is not a separate entity, segment or division; and permitting greater use of pro forma financial statements for purposes of measuring "significance".

Timing of Measurement of the "Investment" Test. As proposed to be revised, the "investment test" for "significance" in Rule 102(w) would be calculated by reference to the acquiror's stock price as of the end of the fiscal year before the transaction occurs. While the end of the fiscal year is a logical time for ascertaining a metric based on the acquiror's balance sheet (as under the current rule) – since it permits use of audited information – this logic does not extend to a market value metric. With a stock price test, no particular date is more reliable than any other, and so it makes more sense to compare amounts that are closer in time to the acquisition announcement. That would seem always to represent the best available information for this purpose, and would also bring the investment test in line with the acquiror's thinking at the time the transaction is decided upon and announced. We therefore suggest a one-time test,

determined once for purposes of any pro forma financial information required to be made in connection with the subject transaction, and measured as of a date or over a period ending on or shortly prior to the announcement of the transaction. This would represent an improvement relative to the proposed rule, and indeed, relative to the current rule, each of which can yield different "significance" results for different filings that must include pro forma information for the same transaction, depending upon the fiscal year in which the calculation is made.

Filed vs. furnished. Given the challenges involved in producing pro forma financial information, discussed above – and particularly if the Commission adds to those challenges by imposing a "Management's Adjustments" requirement – we would urge the Commission to permit Article 11 information to be "furnished" rather than "filed" for all purposes. With that change, acquirors would continue to have potential liability in respect of the pro forma financial information under Rule 10b-5, subject to a "scienter" standard. We think that would represent a more appropriate balancing of the interests of acquirors and investors in this context.

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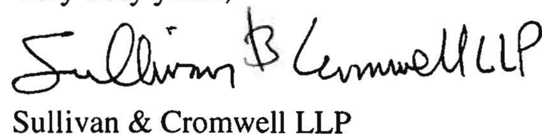
If you would like to discuss our letter, please feel free to contact Melissa Sawyer at [redacted], Eric Krautheimer at [redacted] or Robert Buckholz at [redacted].

Very truly yours,



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