

## LEGAL ALERT

June 2020

**SEC Adopts Amendments to Financial Disclosures about Acquired and Disposed Businesses**

In May 2020, the Securities and Exchange Commission (“**SEC**”) adopted major changes (the “**Amendments**”) to its rules and forms relating to the historical and pro forma financial statements and information that must be provided by public companies in connection with business acquisitions and dispositions.

The Amendments are effective on January 1, 2021. Voluntary early compliance with the Amendments is permitted in advance of the mandatory compliance date provided that the Amendments are applied in their entirety from the date of early compliance.

**Summary of the Amendments**

The Amendments include changes to Regulations S-X and S-K promulgated under the Securities Act of 1933, as amended (the “**Securities Act**”) as well as to certain other SEC rules and forms. The Amendments generally:

- Update the significance tests in Rule 1-02(w) of Regulation S-X, including material changes to the investment test and the income test, which among other matters, determine the financial statement requirements for an acquired business;
- Expand the use of pro forma financial information in measuring significance;
- Conform, to the extent applicable, the significance threshold and tests for a disposed business to those used for an acquired business;
- Require the financial statements of the acquired business to cover only up to the two most recent fiscal years;
- Permit disclosure of abbreviated financial statements for certain acquisitions of a component of an entity;

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We are able to provide counsel and guidance in SEC and New Mining Disclosure matters. For additional information, please contact the attorneys named below or the attorney with whom you have a primary relationship.

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- Permit the use of, or reconciliation to, International Financial Reporting Standards as issued by the International Accounting Standards Board (“**IFRS-IASB**”) in certain circumstances;
- No longer require separate acquired business financial statements once the business has been included in the registrant's post-acquisition audited annual financial statements for either nine months or a complete fiscal year, depending on significance;
- Modify and enhance the required disclosure for the aggregate effect of acquisitions for which financial statements are not required or are not yet required;
- Align Rule 3-14 [applicable to real estate operations] with Rule 3-05 [applicable to non-real estate businesses] where no unique industry considerations exist;
- Amend the pro forma financial information requirements to improve the content and relevance of such information;
- Clarify when financial statements and pro forma financial information are required, and update the language used in the SEC's rules; and
- Make corresponding changes to the smaller reporting company requirements in Article 8 of Regulation S-X.

### **Amendments to the Definition of “Significant Subsidiary” and Generally Applicable Financial Statement Requirements for Acquired Businesses**

The “significant subsidiary” definition in Rule 1-02(w) of Regulation S-X includes investment, asset, and income tests that are applied when determining if a subsidiary is deemed significant for the purposes of certain Regulation S-X and Regulation S-K requirements as well as certain other SEC rules and forms.

#### **Investment Test**

The investment test (the “**Investment Test**”) compares the registrant's and its other subsidiaries' investments in and advances to the tested subsidiary to the total assets of the registrant and its subsidiaries consolidated at the end of the most recently completed fiscal year, or in the case of an acquired business, in the registrant's most recent annual financial statements required to be filed at or prior to the acquisition date.

The Investment Test has been amended to compare the registrant's and its other subsidiaries' investments in and advances to the tested subsidiary to the aggregate worldwide market value of the registrant's voting and non-voting common equity, when available, but this amendment is expressly limited to acquisitions and dispositions. The SEC retained the existing test for acquisitions and dispositions in circumstances where the registrant does not have an aggregate worldwide market value and also retained the existing test when used for certain additional purposes for which the Rule 1-02(w) definition is applicable.

In determining market value, registrants are required to use the average of aggregate worldwide market value calculated daily for the last five trading days of the registrant's most recently completed month ending prior to the earlier of the registrant's announcement date or agreement date of the acquisition or disposition.

The SEC also amended the Investment Test to clarify that for acquisitions, the registrant's and its other subsidiaries' “investments in” the tested subsidiary is the consideration transferred, adjusted to exclude the registrant's and its subsidiaries' proportionate interest in the carrying value of

assets transferred by the registrant and its subsidiaries consolidated to the tested subsidiary that will remain with the combined entity after the acquisition.

The Amendments further provide that the registrant's and its other subsidiaries' "investments in" the tested subsidiary shall include the fair value of contingent consideration if required to be recognized at fair value by the registrant at the acquisition date under U.S. GAAP or IFRS-IASB, as applicable; however if recognition at fair value is not required, it shall include all contingent consideration, except contingent consideration for which the likelihood of payment is remote.

## **Income Test**

The income test (the "**Income Test**") compares the registrant's equity in the tested subsidiary's income from continuing operations before income taxes exclusive of amounts attributable to any noncontrolling interests to such income of the registrant for the most recently completed fiscal year. In the case of an acquisition, the Income Test similarly compares the registrant's equity in the income from continuing operations of the acquired business before income taxes, exclusive of amounts attributable to any noncontrolling interests, as reflected in the business's most recent annual pre-acquisition financial statements, to the same measure of the registrant reflected in its most recent annual financial statements required to be filed at or prior to the acquisition date.

The Income Test has been revised to add a revenue component in order to reduce the anomalous result that registrants with marginal or break-even net income or loss in a recent fiscal year may be more likely to have tested subsidiaries deemed significant where they otherwise would not. To satisfy the revised Income Test, the tested subsidiary must meet both the revenue component and the net income component when the revenue component applies, and for purposes of the application of Rule 3-05, may use the lower of the revenue component and the net income component to determine the number of periods for which Rule 3-05 Financial Statements are required.

The new revenue component compares a registrant's and its other subsidiaries' proportionate share of the tested subsidiary's consolidated total revenues (after intercompany eliminations) to such consolidated total revenues of the registrant for the most recently completed fiscal year. However, the revenue component does not apply if either the registrant and its subsidiaries consolidated or the tested subsidiary did not have material revenue in each of the two most recently completed fiscal years.

## **Other Changes**

Under the Amendments, registrants will use the revised Income Test, but will continue to use the existing Investment Test for testing significance of equity method investees under Rules 3-09 and 4-08(g) of Regulation S-X, as well as for certain other purposes for which the definition is used.

## **Audited Financial Statements for Significant Acquisitions**

Rule 3-05 of Regulation S-X has been revised to require a maximum of two years of audited historical financial statements of the target company rather than three. In addition, Rule 3.05 has been amended for acquisitions where a significance test exceeds 20 percent, but none exceeds 40 percent, to require financial statements for the "most recent" interim period specified in Rules

3-01 and 3-02 rather than “any” interim period. The revision eliminates the need to provide a comparative interim period when only one year of audited Rule 3-05 Financial Statements is required.

### **Financial Statements for Net Assets that Constitute a Business**

Registrants frequently acquire a component of an entity that is a business as defined in Rule 11-01(d) of Regulation S-X but does not constitute a separate entity, subsidiary, or division, such as a product line or a line of business contained in more than one subsidiary of the selling entity. These businesses may not have separate financial statements or maintain separate and distinct accounts necessary to prepare Rule 3-05 Financial Statements because they often represent only a small portion of the selling entity. In these circumstances, making relevant allocations of the selling entity’s corporate overhead, interest, and income tax expenses necessary to provide Rule 3-05 Financial Statements may be impracticable and the SEC staff has permitted registrants to instead provide audited abbreviated financial statements of the acquired business in the form of statements of assets acquired and liabilities assumed and statements of revenues and expenses.

The Amendments include revisions to Rule 3-05(e) of Regulation S-X that permit registrants to provide audited abbreviated financial statements in the form of statements of assets acquired and liabilities assumed, and statements of revenues and expenses (exclusive of corporate overhead, interest and income tax expenses) if the acquired business meets certain qualifying and presentation conditions.

The Amendments do not apply to “carve-out financial statements.” The SEC staff believes that questions relating to carve-out financial statements are best addressed on the basis of their unique facts and circumstances through the staff consultation process.

### **Foreign Businesses**

Regulation S-X permits the use of IFRS-IASB without reconciliation to U.S. GAAP in financial statements of foreign private issuers. Rule 3-05 similarly permits the use of IFRS-IASB in financial statements of foreign businesses. However, if Rule 3-05 Financial Statements of a foreign business are prepared on a basis of accounting other than U.S. GAAP or IFRS-IASB, such as home-country GAAP, the Rule 3-05 Financial Statements are required to be reconciled to U.S. GAAP even if the registrant is a foreign private issuer that prepares its financial statements in accordance with IFRS-IASB.

Further, while the definitions of “foreign private issuer” and “foreign business” have similarities, they have different ownership requirements such that a business could qualify to be a “foreign private issuer” if it were a registrant, but not qualify to be a “foreign business” when it is acquired by a registrant. In this circumstance, a registrant acquiring such a business is not permitted to present Rule 3-05 Financial Statements of the acquired business prepared in accordance with IFRS-IASB, even when those financial statements are already available and even though the acquired business could present IFRS-IASB financial statements if it were a registrant. Instead, the Rule 3-05 Financial Statements must be prepared in accordance with U.S. GAAP.

The Amendments revise Rule 3-05(c) to permit foreign private issuers that prepare their financial statements using IFRS-IASB to reconcile Rule 3-05 Financial Statements of foreign businesses

prepared using home country GAAP to IFRS-IASB rather than U.S. GAAP. The reconciliation to IFRS-IASB is required generally to follow the form and content requirements in Item 17(c) of Form 20-F.

Additionally, Rule 3-05(d) has been revised to permit Rule 3-05 Financial Statements to be prepared in accordance with IFRS-IASB without reconciliation to U.S. GAAP if the acquired business would qualify as a foreign private issuer if it were a registrant. In circumstances where the registrant presents its financial statements in U.S. GAAP, the pro forma financial information reflecting the acquisition will continue to be required to be presented in U.S. GAAP.

The Amendments permit an acquired business that would qualify as a foreign private issuer if it were a registrant to reconcile to IFRS-IASB rather than U.S. GAAP when the registrant is a foreign private issuer that uses IFRS-IASB.

### **Smaller Reporting Companies and Issuers Relying on Regulation A**

Rule 8-04 of Regulation S-X provides smaller reporting company disclosure requirements for the financial statements of businesses acquired or to be acquired. Part F/S of Form 1-A (“**Part F/S**”) directs an issuer relying on Regulation A to present financial statements of businesses acquired or to be acquired, as specified by Rule 8-04 of Regulation S-X, but permits the periods presented to be the shorter of those applicable to issuers relying on Regulation A and the periods specified by Article 8.

Rule 8-04 has been revised to reference to Rule 3-05 for the requirements relating to the financial statements of businesses acquired or to be acquired, other than for form and content requirements for such financial statements, which would continue to be prepared in accordance with Rules 8-02 and 8-03 of Regulation S-X.

As revised, Rule 8-04 continues to require up to two years of acquired business historical financial statements. Additionally, and in accordance with current practice, the revised rule expressly permits smaller reporting companies to omit such financial statements if the acquired business has been included in the registrant's results for a complete fiscal year. The Amendments also expressly permit smaller reporting companies to file audited financial statements covering a period of nine to 12 months to satisfy the requirement for filing financial statements for a period of one year for an acquired business.

The Amendments also provide that a smaller reporting company is eligible to exclude acquired business financial statements from a registration statement if the business acquisition was consummated no more than 74 days prior to the date of the relevant final prospectus or prospectus supplement, rather than 74 days prior to the effective date of the registration statement as under current Rule 8-04(c)(4).

### **Amendments Relating to Rule 3-05 Financial Statements Included in Registration Statements and Proxy Statements**

## **Omission of Rule 3-05 Financial Statements for Businesses That Have Been Included in the Registrant's Financial Statements**

Rule 3-05(b)(4)(iii) of Regulation S-X generally permits Rule 3-05 Financial Statements to be omitted once the operating results of the acquired business have been reflected in the audited consolidated financial statements of the registrant for a complete fiscal year. However, Rule 3-05 Financial Statements are required to be included when they have not been previously filed, or when the Rule 3-05 Financial Statements have been previously filed but the acquired business is of major significance to the registrant.

If Rule 3-05 Financial Statements have not been previously filed, they must be provided even if the acquired business is included in post-acquisition audited results. The staff has historically not objected, however, to registrants reducing the Rule 3-05 Financial Statement periods presented by the equivalent period that the acquired business is included in the registrant's post-acquisition audited results.

Under the current Rules, registrants must also continue to present Rule 3-05 Financial Statements that have been previously filed if the acquired business is of such significance to the registrant that omission of those Rule 3-05 Financial Statements would materially impair an investor's ability to understand the historical financial results of the registrant. Rule 3-05 provides, as an example, that an acquired business meeting at least one of the significance tests set forth in Rule 1-02(w) at the 80 percent level at the date of the acquisition would require the registrant to continue to file the financial statements of the acquired business.

The Amendments eliminate the requirement to include Rule 3-05 Financial Statements in registration statements and proxy statements once the acquired business is reflected in filed post-acquisition registrant financial statements.

In addition, the Amendments allow omission of pre-acquisition financial statements for businesses that exceed 20 percent but do not exceed 40 percent significance once they are included in the registrant's audited post-acquisition results for nine months (rather than the complete fiscal year).

The Amendments also eliminate the requirement that Rule 3-05 Financial Statements be provided when they have not been previously filed or when they have been previously filed but the acquired business is of major significance.

## **Use of Pro Forma Financial Information to Measure Significance**

A registrant is generally permitted to use pro forma, rather than historical, financial information to test significance of a subsequently acquired business if the registrant made a significant acquisition after the latest fiscal year-end and filed its Rule 3-05 Financial Statements and pro forma financial information on Form 8-K. However, this Form 8-K filing requirement has the practical effect of precluding the use of pro forma financial information that gives effect to a significant acquisition subsequent to the latest fiscal year-end to test significance of a subsequently acquired business when determining Rule 3-05 disclosure requirements in initial registration statements. Further, Regulation S-X does not provide for dispositions of significant businesses to be included in the pro forma financial information used for testing significance of a subsequently acquired or subsequently disposed business.

The SEC has amended Rule 11-01(b)(3) of Regulation S-X to permit registrants to measure significance using filed pro forma financial information that only depicts significant business acquisitions and dispositions consummated after the latest fiscal year-end for which the registrant's financial statements are required to be filed, subject to the following conditions:

- The registrant has filed Rule 3-05 Financial Statements or Rule 3-14 Financial Statements for any such acquired business; and
- The registrant has filed the pro forma financial information required by Article 11 for any such acquired or disposed business.

The Amendments include additional guidelines for the use of pro forma financial information for such purpose. Once a registrant uses pro forma financial information to measure significance, it must continue to use pro forma financial information to measure significance until the next annual report on Form 10-K or Form 20-F.

### **Disclosure Requirements for Individually Insignificant Acquisitions**

Under the existing rules, audited historical pre-acquisition financial statements are generally not required if an acquired or to be acquired business: (1) does not exceed 20 percent significance, or (2) does not exceed 50 percent significance and the acquisition has not yet occurred or the date of the final prospectus or prospectus supplement relating to an offering (as filed with the Commission pursuant to 17 CFR 230.424(b)) is no more than 74 days after consummation and the financial statements have not been previously filed.

However, if the aggregate impact of "individually insignificant businesses" acquired since the date of the most recent audited balance sheet filed for the registrant exceeds 50 percent, audited historical pre-acquisition financial statements covering at least the substantial majority of the businesses acquired must be included in a registration statement or proxy statement. Registrants also must provide related pro forma financial information based on the requirements of Article 11.

The SEC has amended Rule 3-05(b)(2)(iv) of Regulation S-X to clarify that "individually insignificant businesses" include: (a) Any acquisition consummated after the registrant's audited balance sheet date whose significance does not exceed 20 percent; (b) Any probable acquisition whose significance does not exceed 50 percent; and (c) Any consummated acquisition whose significance exceeds 20 percent, but does not exceed 50 percent, for which financial statements are not yet required by Rule 3-05(b)(4) because of the 75-day filing period.

In conjunction with this change, the amended rule will require registrants to provide pro forma financial information depicting the aggregate effects of all "individually insignificant businesses" in all material respects. Further, Rule 11-01(c) has been amended to clarify that the exception that would otherwise permit pro forma financial information not to be provided when separate financial statements of the acquired business are not included in the filing does not apply where the aggregate impact is significant as determined by amended Rules 3-05(b)(2)(iv) or 3-14(b)(2)(i)(C).

In determining whether the Income Test condition (*i.e.* both the revenue component and the net income component) exceeds 50 percent, the businesses specified in Rule 3-05(b)(2)(iv) reporting

losses must be aggregated separately from those reporting income. If either group exceeds 50 percent, the disclosure requirements apply to all of the businesses subject to the aggregate test and must not be limited to either the businesses with losses or those with income.

### **Rule 3-14 - Financial Statements of Real Estate Operations Acquired or to be Acquired**

Rule 3-14 of Regulation S-X governs the financial statements requirements in connection with the acquisition or disposition of significant real estate operations. Currently, there are a number of differences between the requirements under Rules 3-14 and 3-05. Under the Amendments, the requirements of these sections have been substantially aligned with certain continuing differences, which are outside the scope of this Legal Alert.

### **Pro Forma Financial Information**

The pro forma financial information described in Article 11 of Regulation S-X must accompany Rule 3-05 Financial Statements and Rule 3-14 Financial Statements. Typically, pro forma financial information includes the most recent balance sheet and most recent annual and interim period income statements. Pro forma financial information for a business acquisition combines the historical financial statements of the registrant and the acquired business and is adjusted for certain items if specified criteria are met.

### **Adjustment Criteria and Presentation Requirements**

Rule 11-02 of Regulation S-X contains rules and instructions for the presentation of pro forma financial information. Article 11 of Regulation S-X provides that the only adjustments that are appropriate in the presentation of the pro forma condensed statement of comprehensive income are those that are:

- Directly attributable to the transaction;
- Expected to have a continuing impact on the registrant; and
- Factually supportable.

The pro forma condensed balance sheet, on the other hand, reflects pro forma adjustments that are directly attributable to the transaction and factually supportable, regardless of whether the impact is expected to be continuing or nonrecurring because the objective of the pro forma balance sheet is to reflect the impact of the transaction on the financial position of the registrant as of the balance sheet date.

The SEC has amended Article 11 by replacing the existing pro forma adjustment criteria with simplified requirements to depict the accounting for the transaction and to provide the option to depict synergies and dis-synergies of the acquisitions and dispositions for which pro forma effect is being given.

The revised pro forma adjustment criteria are broken out into three categories:

- (i) **“Transaction Accounting Adjustments;”**
- (ii) **“Autonomous Entity Adjustments;”** and
- (iii) **“Management’s Adjustments.”**



**Transaction Accounting Adjustments** reflect only the application of required accounting to the acquisition, disposition, or other transaction linking the effects of the acquired business to the registrant's audited historical financial statements.

**Autonomous Entity Adjustments** are adjustments necessary to reflect the operations and financial position of the registrant as an autonomous entity when the registrant was previously part of another entity.

**Management's Adjustments** provide both flexibility to registrants to include forward-looking information that depicts the synergies and dis-synergies identified by management in determining to consummate or integrate the transaction for which pro forma effect is being given and insight to investors into the potential effects of the acquisition and the post-acquisition plans expected to be taken by management.

Under the Amendments, Transaction Accounting Adjustments and Autonomous Entity Adjustments are required adjustments. Management's Adjustments, as discussed further below, are optional.

#### *Transaction Accounting Adjustments and Autonomous Entity Adjustments*

Amended Rule 11-02(a)(6)(i) requires registrants to depict: (1) in the pro forma condensed balance sheet the accounting for the transaction required by U.S. GAAP or IFRS-IASB, as applicable, and (2) in the pro forma condensed income statements, the effects of those pro forma balance sheet adjustments assuming the adjustments were made as of the beginning of the fiscal year presented. If the condition in Rule 11-01(a) that is met does not have a balance sheet effect, then the Transaction Accounting Adjustments to the pro forma statement of comprehensive income should depict the accounting for the transaction required by U.S. GAAP or IFRS-IASB, as applicable.

The requirement to show the registrant as an autonomous entity if the condition in Rule 11-01(a)(7) is met has been relabeled as "Autonomous Entity Adjustments" and they must be presented in a separate column from Transaction Accounting Adjustments.

The Amendments will require that historical and pro forma per share data must be presented on the face of the pro forma condensed statement of comprehensive income and give effect to Transaction Accounting Adjustments. The amendments require that such pro forma per share data also give effect to Autonomous Entity Adjustments.

#### *Management's Adjustments*

The Amendments provide that Management's Adjustments depicting synergies and dis-synergies of the acquisitions and dispositions for which pro forma financial information is being given may, in the registrant's discretion, be presented if in its management's opinion, such adjustments would enhance an understanding of the pro forma effects of the transaction. In order to present Management's Adjustments, certain conditions related to the basis for Management's Adjustments and the form of presentation must be met. The *Basis for Management's Adjustments* in Rule 11-02(a)(7)(i) requires as conditions for presenting Management's Adjustments that:

- There is a reasonable basis for each such adjustment;

- The adjustments are limited to the effect of such synergies and dis-synergies on the historical financial statements that form the basis for the pro forma statement of comprehensive income as if the synergies and dis-synergies existed as of the beginning of the fiscal year presented. If such adjustments reduce expenses, the reduction shall not exceed the amount of the related expense historically incurred during the pro forma period presented; and
- The pro forma financial information reflects all Management's Adjustments that are, in the opinion of management, necessary to a fair statement of the pro forma financial information presented and a statement to that effect is disclosed. When synergies are presented, any related dis-synergies shall also be presented.

Further, as modified, the *Form of Presentation* in Rule 11-02(a)(7)(ii) requires as additional conditions for presenting Management's Adjustments that:

- If presented, Management's Adjustments must be presented in the explanatory notes to the pro forma financial information in the form of reconciliations of pro forma net income from continuing operations attributable to the controlling interest and the related pro forma earnings per share data to such amounts after giving effect to Management's Adjustments.
- If presented, Management's Adjustments included or incorporated by reference into a registration statement, proxy statement, offering statement or Form 8-K should be as of the most recent practicable date prior to the effective date, mail date, qualified date, or filing date as applicable, which may require that they be updated if previously provided in a Form 8-K that is appropriately incorporated by reference.
- If Management's Adjustments will change the number of shares or potential common shares, the change must be reflected within Management's Adjustments in accordance with U.S. GAAP or IFRS-IASB, as applicable, as if the common stock or potential common stock were outstanding as of the beginning of the period presented.

The explanatory notes must also include disclosure of the basis for and material limitations of each Management's Adjustment, including any material assumptions or uncertainties of such adjustment, an explanation of the method of the calculation of the adjustment, if material, and the estimated time frame for achieving the synergies and dis-synergies of such adjustment.

Because Management's Adjustments might contain forward-looking information, the amended Rule includes an instruction indicating that any forward-looking information supplied is expressly covered by the safe harbor provisions under 17 CFR 230.175 and 17 CFR 240.3b-6.

### *Explanatory Notes*

To further clarify the pro forma financial information disclosure, the Amendments will require disclosure of revenues, expenses, gains and losses, and related tax effects that will not recur in the income of the registrant beyond 12 months after the transaction. Additionally, for Transaction Accounting Adjustments, the Amendments will require disclosure of:

- Total consideration transferred or received, including its components and how they were measured. If total consideration includes contingent consideration, the Amendments will require disclosure of the contingent consideration arrangement(s), the basis for determining the amount of payment(s) or receipt(s), and an estimate of the range of

outcomes (undiscounted) or, if a range cannot be estimated, that fact and the reasons why; and

- When the initial accounting is incomplete: a prominent statement to this effect, the items for which the accounting depicted is incomplete, a description of the information that the registrant requires, including, uncertainties affecting the pro forma financial information and the possible consequences of their resolution, an indication of when the accounting is expected to be finalized, and other available information regarding the magnitude of any potential adjustments.

The Amendments provide that the accompanying explanatory notes shall disclose for each Autonomous Entity Adjustment, a description of the adjustment (including the material uncertainties), the material assumptions, the calculation of the adjustment, and qualitative information about the Autonomous Entity Adjustments necessary to give a fair and balanced presentation of the pro forma financial information.

### *Significance and Business Dispositions*

Rule 11-01(a)(4) provides that pro forma financial information is required upon the disposition or probable disposition of a significant portion of a business either by sale, abandonment, or distribution to shareholders by means of a spin-off, split-up, or split-off, if that disposition is not fully reflected in the financial statements of the registrant. Rule 11-01(b) further provides that a disposition of a business is significant if the business to be disposed of meets the conditions of a significant subsidiary under Rule 1-02(w). Rule 1-02(w) uses a 10 percent significance threshold, rather than the 20 percent threshold used for business acquisitions under Rules 3-05 and 11-01(b).

When a registrant determines that it has an acquisition or disposition of a significant amount of assets that do not constitute a business, Item 2.01 of Form 8-K uses a 10 percent threshold for both acquisitions and dispositions to require disclosure of certain details of the transaction. The terms “business” and “significant” used in Form 8-K specifically reference Article 11 of Regulation S-X.

Rule 11-01(b) has been amended to raise the significance threshold for the disposition of a business from 10 percent to 20 percent and to conform, to the extent applicable, the tests used to determine significance of a disposed business to those used to determine significance of an acquired business. Form 8-K and Article 8 have also been amended to require smaller reporting companies to provide pro forma financial information for disposition of a significant business in Form 8-K and in certain registration statements and proxy statements when the disposition occurs during or after the most recently completed fiscal year.

### **Smaller Reporting Companies and Issuers Relying on Regulation A**

Rule 8-05 of Regulation S-X sets forth pro forma financial information requirements for business acquisitions by smaller reporting companies. Additionally, Part F/S of Form 1-A directs an issuer relying on Regulation A to present the pro forma financial information specified by Rule 8-05. Like Article 11, Rule 8-05(a) requires pro forma financial information only if financial statements of a business acquired or to be acquired are presented. Like Article 11, Rule 8-05(b) provides that pro forma financial information must consist of a pro forma balance sheet and a pro forma statement of comprehensive income presented in condensed, columnar form for the most recent year and interim period. Rule 8-05(b), however, does not provide further preparation

guidance, such as the types of pro forma adjustments that can be made. Note 2 of the Preliminary Notes to Article 8 provides that, to the extent that Article 11-01 offers enhanced guidelines for the preparation, presentation, and disclosure of pro forma financial information, smaller reporting companies may wish to consider these items.

The SEC has revised Rule 8-05 to require that the preparation, presentation, and disclosure of pro forma financial information by smaller reporting companies substantially comply with Article 11. Additionally, because Part F/S of Form 1-A refers to Rule 8-05, the amendments to Rule 8-05 will apply to issuers relying on Regulation A.

## **Transition**

Registrants will not be required to apply the Amendments until the beginning of a registrant's fiscal year beginning after December 31, 2020 (the "**mandatory compliance date**"). Acquisitions and dispositions that are probable or consummated after the mandatory compliance date must be evaluated for significance using the Amendments.

Registrants filing initial registration statements are not required to apply the Amendments until an initial registration statement is first filed on or after the mandatory compliance date. For initial registration statements first filed on or after the mandatory compliance date, all probable or consummated acquisitions and dispositions, including those consummated prior to the mandatory compliance date, must be evaluated for significance using the Amendments.

Voluntary early compliance with the Amendments is permitted in advance of the registrant's mandatory compliance date provided that the Amendments are applied in their entirety from the date of early compliance.

Additional Information about the Amendments is available in the SEC's Adopting Release (No. 33-10786: May 20, 2020): <https://www.sec.gov/rules/final/2020/33-10786.pdf>