

**SEC Regulations Committee**  
**July 10, 2007 - Joint Meeting with SEC Staff**  
**SEC Offices – Washington DC**

**Discussion Document A**

**Topic: Reporting Requirements of Rule 4-08(g) of Regulation S-X for Periods in which the Investee is Less than 10% Significant**

**Issue:** If an investee meets the significance threshold for including summarized financial data under Rule 4-08(g) of Regulation S-X in the current year but not in the prior year (or vice versa), must all periods be presented in the notes to the annual financial statements?

**Background:** Rule 4-08(g) of Regulation S-X requires disclosure of summarized financial information if an investee or any group of investees meets the definition of a significant subsidiary specified in Rule 1-02(w) (i.e., greater than 10% significant). Rule 4-08(g)(2) states that "the information shall be presented insofar as is practicable as of the same dates and for the same periods as the audited consolidated financial statements...".

Consider the following example:

Company X owns 30% of the common equity of Investee I and 40% of the common equity of Investee J. Company X accounts for its investments in both investees under the equity method of accounting. In connection with the preparation of its Form 10-K for the year ended December 31, 2006, Company X has determined the significance of Investee I and Investee J. In each year, the income test yielded the greatest level of significance as follows:

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Investee I	7%	2%	1%
Investee J	<u>5%</u>	<u>1%</u>	<u>3%</u>
	<u>12%</u>	<u>3%</u>	<u>4%</u>

There are no qualitative factors which suggest that the information for 2005 and 2004 would be material to an investor.

**Question 1:** For what periods is Company X required to provide summarized financial information under Rule 4-08(g)?

**View A:** Company X is required to present summarized balance sheet financial information for 2006 and 2005 and summarized income statement information for 2006, 2005 and 2004. This is true even though the investees only exceeded the significance threshold in 2006. None of the periods may be provided on an unaudited basis.

**View A-1:** Same as View A, except, consistent with the provisions of Rule 3-09, Company X may present the information on an unaudited basis for years in which the investees did not exceed the significance threshold.

**View B:** Absent any qualitative factors that make the 2005 and 2004 information material to investors, Company X is only required to present summarized financial information for 2006 because that is the only year for which the investees exceeded the significance threshold. If there are qualitative characteristics relating to the 2005 and 2004 summarized financial data that would make that information material to an investor, the registrant should provide that information.

**Committee Recommendation:** The Committee supports View B. If the registrant concludes that the comparative information for 2005 and 2004 is not material, then it need not be presented. However, a registrant could elect to include the information for additional periods (i.e., 2005 and 2004) on either an audited or unaudited basis for comparative purposes.

**SEC Staff Response:** The staff supports View A.

**Question 2:** For what periods would Company X be required to provide (in its 2006 Form 10-K) summarized financial information under Rule 4-08(g) if the significance tests were as follows:

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Investee I	1%	5%	2%
Investee J	<u>3%</u>	<u>7%</u>	<u>1%</u>
	<u>4%</u>	<u>12%</u>	<u>3%</u>

There are no qualitative factors which suggest that the information for 2006 and 2004 would be material to an investor.

**View A:** Company X is required to present summarized balance sheet financial information for 2006 and 2005 and summarized income statement information for 2006, 2005 and 2004. This is true even though the investees only exceeded the significance threshold in 2005. None of the periods may be provided on an unaudited basis.

**View A-1:** Same as View A, except, consistent with the provisions of Rule 3-09, Company X may present the information on an unaudited basis for years in which the investees did not exceed the significance threshold.

**View B:** Absent any qualitative factors that make the 2006 and 2004 information material to investors, Company X is only required to present summarized financial information for 2005 because that is the only year for which the investees exceeded the significance threshold. If there are qualitative characteristics relating to the 2006 and 2004 summarized financial data that would make that information material to an investor, the registrant should provide that information.

**View C:** Company X is not required to provide any summarized information pursuant to Rule 4-08(g) because the investees were not significant in the most recent fiscal year.

**Committee Recommendation:** The Committee supports View B. If the registrant concludes that the comparative information for 2006 and 2004 is not material, then it need not be presented. However, a registrant could elect to include the information for additional periods (i.e., 2006 and 2004) on either an audited or unaudited basis for comparative purposes.

**SEC Staff Response:** The staff supports View A.

**Question 3:** For what periods would Company X be required to provide (in its 2006 Form 10-K) summarized financial information under Rule 4-08(g) if the significance tests were as follows:

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Investee I	1%	2%	5%
Investee J	<u>3%</u>	<u>1%</u>	<u>7%</u>
	<u>4%</u>	<u>3%</u>	<u>12%</u>

There are no qualitative factors which suggest that the information for 2006 and 2005 would be material to an investor.

**View A:** Company X is required to present summarized balance sheet financial information for 2006 and 2005 and summarized income statement information for 2006, 2005 and 2004. This is true even though the investees only exceeded the significance threshold in 2004. None of the periods may be provided on an unaudited basis.

**View A-1:** Same as View A, except, consistent with the provisions of Rule 3-09, Company X may present the information on an unaudited basis for years in which the investees did not exceed the significance threshold.

**View B:** Absent any qualitative factors that make the 2006 and 2005 information material to investors, Company X is only required to present summarized financial information for 2004 because that is the only year for which the investees exceeded the significance threshold. If there are qualitative characteristics relating to the 2006 and 2005 summarized financial data that would be made that information material to an investor, the registrant should provide that information.

**View C:** Company X is not required to provide any summarized information pursuant to Rule 4-08(g) because the investees were not significant in the most recent fiscal year.

**View C-1:** Summarized financial information under SX 4-08(g) need not be presented in the 2006 Form 10-K because complete financial statements are not presented for 2004, (i.e., the 2004 financial statements are incomplete because they do not include a 2004 balance sheet). The 2004 income statement and statements of cash flows and shareholders' equity are presented for comparative purposes to the 2005 and 2006 financial statements. Accordingly, if the investees are only significant in 2004, summarized financial information need not be provided in the 2006 Form 10-K.

**Committee Recommendation:** The Committee supports View B. If the registrant concludes that the information for 2006 and 2005 is not material, then it need not be presented. However, a registrant could elect to include the information for additional periods (i.e., 2006 and 2005) on either an audited or unaudited basis for comparative purposes.

**SEC Staff Response:** The staff supports View A.