

# Legal Update

## SEC Amends Requirements for Statistical Disclosures for Bank and Savings and Loan Registrants, Replacing Industry Guide 3

On September 11, 2020, the U.S. Securities and Exchange Commission (SEC) adopted, in substantially the form it had proposed, amendments to the requirements for statistical disclosures that bank and savings and loan registrants provide to investors.<sup>1</sup>

The rules rescind Industry Guide 3, *Statistical Disclosure by Bank Holding Companies* (Guide 3);<sup>2</sup> codify certain Guide 3 disclosures into a new Subpart 1400 of Regulation S-K, eliminate other Guide 3 disclosures that overlap with other SEC disclosure requirements, U.S. Generally Accepted Accounting Principles (GAAP) or International Financial Reporting Standards (IFRS); and add certain credit ratio disclosure requirements.

According to the SEC, the rules aim to streamline compliance efforts and decrease reporting burdens for registrants and to enhance comparability among issuers. The changes also form part of the SEC's Division of Corporation Finance's (CorpFin) disclosure effectiveness initiative.

### Background

Guide 3 was first published in 1976 as a "convenient reference" to the statistical disclosures sought by CorpFin in registration statements and other

disclosure documents filed by bank holding companies (BHCs).<sup>3</sup> Guide 3 calls for statistical disclosures related to interest-earning assets and interest-bearing liabilities of BHCs. These disclosures were designed to assist investors in evaluating loan portfolio risk characteristics, among other risks, to BHCs. Guide 3 disclosures are commonly found in tabular form in the Description of Business or Management's Discussion and Analysis (MD&A) sections of a BHC registrant's SEC filings.

While Guide 3 has been amended on a few occasions, its last substantive revision was more than 30 years ago, in 1986. Since then, a number of significant financial reporting changes have occurred, including the issuance of new accounting standards by the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB). In addition, especially since the financial crisis, the banking agencies have adopted a number of disclosure requirements for BHCs. Hence, in March 2017, the SEC published a request for comment seeking public input on possible changes to Guide 3.<sup>4</sup> It noted that the financial services industry has dramatically changed since Guide 3 was published and that, consequently, existing guidance may not always reflect recent industry developments or changes in accounting

standards related to financial and reporting requirements. The SEC published a proposing release on September 17, 2019 seeking comments on proposal amendments to Guide 3. Generally, the comments on the proposing release supported the changes. Below we summarize the key elements of the final rules.

## Codification, Elimination and Addition

Certain Guide 3 disclosures will be updated and codified into a new Subpart 1400 of Regulation S-K. At present, Guide 3 and other industry guides do not constitute SEC rules, nor do they bear official SEC approval. Rather, they represent disclosure policies and practices followed by CorpFin to administer the federal securities laws and are intended to assist registrants and their counsel in preparing disclosures. The SEC's final rules would elevate the required disclosures from CorpFin guidance to SEC rules.

The final rules would *not* codify a number of Guide 3 disclosure items that currently overlap with existing SEC rules, GAAP or IFRS, in effect eliminating these Guide 3 disclosure requirements.

## Scope and Applicability

### ENTITIES COVERED

Subpart 1400 applies to a bank, bank holding company, savings and loan association, or savings and loan holding company (collectively, bank and savings and loan registrants).

### DOMESTIC AND FOREIGN REGISTRANTS

Subpart 1400 applies to both domestic registrants and foreign registrants. There are no specific accommodations for issuers that report in IFRS.

Rule 409 under the Securities Act of 1933 and Rule 12b-21 under the Securities Exchange Act of 1934 currently allow registrants, not just foreign registrants, to seek relief from providing information that is "unknown and not reasonably available to the

registrant" or would involve "unreasonable effort or expense." To the extent that a foreign registrant that reports in IFRS encounters difficulties, it can rely on these rules in order to seek relief as needed.

### REPORTING PERIOD

Subpart 1400 reduces the reporting periods previously required under Guide 3 and aligns them with the relevant annual periods required by SEC rules for a registrant's financial statements.

Guide 3 requires BHCs to provide statistical disclosures for each "reported period." Guide 3 defines "reported period" as (i) *five years* of loan portfolio and summary of loan loss experience data, (ii) *three years* for all other information, except that, (iii) for all types of information (including under items (i) and (ii) above), registrants with less than \$200 million of assets or \$10 million or less of net worth may choose to present only *two years* of the required information. "Reported period" includes any additional interim period "necessary to keep the information from being misleading," and such additional interim period should be included "if a material change in the information presented or the trend evidenced thereby has occurred."

Under Subpart 1400, "reported period" is now defined as (1) for all disclosures, *each annual period* required by SEC rules for a registrant's financial statements and (2) any additional interim period subsequent to the most recent fiscal year-end if a material change in the information presented or the trend evidenced thereby has occurred. The SEC did not adopt the proposals that would have required certain credit ratio disclosures for each of the registrant's last five fiscal years in initial registration statements or offering statements. The final rules limit the required credit ratio disclosures to the periods for which financial statements are required.

As a result, Subpart 1400 generally reduces the reporting periods and aligns them with the number of years required by Regulation S-X to be presented in a registrant's financial statements.

## DISCLOSURE AREAS COVERED

Guide 3 covers seven disclosure areas: (1) distribution of assets, liabilities and stockholders' equity; interest rates; and interest differential; (2) investment portfolio; (3) loan portfolio; (4) summary of loan loss experience; (5) deposits; (6) return on equity and assets; and (7) short-term borrowings.

In contrast, Subpart 1400 is organized as follows and covers five disclosure areas identified by Items 1402 to 1406 below.

### Subpart 1400 — Disclosure by Bank and Savings and Loan Registrants

Item 1401. General Instructions

Item 1402. Distribution of assets, liabilities and stockholders' equity; interest rates; and interest differential.

Item 1403. Investments in debt securities.

Item 1404. Loan portfolio.

Item 1405. Allowance for Credit Losses.

Item 1406. Deposits.

### Item 1402: Distribution of Assets, Liabilities and Stockholders' Equity; Interest Rates; and Interest Differential

Item 1402 codifies the requirements currently required by disclosure area Item I of Guide 3.

For each reported period, the registrant must present average balance sheets, which may be condensed from consolidated financial statements, provided that the condensed average balance sheets indicate the significant categories of assets and liabilities, including all major categories of interest-earning assets and interest-bearing liabilities. Major categories of interest-earning assets must include, if material, loans, taxable investment securities, non-taxable investment securities, interest-bearing deposits in other banks, federal funds sold, securities purchased with agreements to resell and other short-term investments. Major categories of

interest-bearing liabilities must include, if material, savings deposits, other time deposits, federal funds purchased, securities sold under agreements to repurchase, commercial paper, other short-term debt and long-term debt.

For each period, the registrant must present an analysis of net interest earnings as follows:

- (1) for each major category of interest-earning asset and each major category of interest-bearing liability, the average amount outstanding during the period and the interest earned or paid on such amount;
- (2) the average yield for each major category of interest-earning assets;
- (3) the average rate paid for each major category of interest-bearing liabilities;
- (4) the average yield on all interest-earning assets and the average rate paid on all interest-bearing liabilities;
- (5) the net yield on interest-earning assets; and
- (6) at the registrant's option, its analysis in connection with the average balance sheet that is required by this rule.

For the interest rates and interest differential analysis, the registrant must provide certain disaggregated disclosures.

### Item 1403: Investments in Debt Securities

Item 1403 streamlines a number of the investment portfolio disclosures currently required by Item II of Guide 3 so that the relevant disclosure Item required will now be the "weighted average yield of each category of debt securities not carried at fair value through earnings" for which disclosure is required in the financial statements, presented for a specified range of maturities (e.g., due one year or less, within five years, within five to ten years, and after ten

years). The registrant must also disclose how the weighted average yield has been calculated.

Item 1403 does not codify a number of the investment portfolio disclosures currently required by Item II of Guide 3, such as book value information, maturity analysis of book value information, and disclosures related to investments exceeding 10 percent of stockholders' equity (e.g., issuer name, aggregate book value and aggregate market value of issuer's securities).

These disclosures substantially overlap with GAAP and IFRS requirements.

### Item 1404: Loan Portfolio

Item 1404 streamlines a number of the loan portfolio disclosures currently required by Item III of Guide 3. The following disclosure sub-items are currently called for under Item III of Guide 3: (a) types of loans (e.g., domestic or foreign; commercial, real estate-construction, real estate-mortgage; governments and official institutions, banks and other financial institutions, other loans, etc.), (b) maturities and sensitivities of loans to changes in interest rates, (c) risk elements and (d) other interest-bearing assets.

Item 1404 does *not* codify Item III.A - loan category disclosures, Item III.C - loan portfolio risk elements and Item III.D - other interest-bearing assets, all required by Guide 3. The SEC reasoned that similar disclosures are already required under SEC rules, GAAP and IFRS.

Item 1404 codifies the maturity by loan category disclosure required by Item III.B of Guide 3, but the loan categories are based on the loan categories required to be disclosed in the registrant's GAAP or IFRS financial statements that are due in one year or less, after one year through five years, after five years through 15 years and after 15 years.

Item 1404 also requires, for each loan category above, to present separately the total amount of loans in each such loan category that are due after

one year that have predetermined interest rates and that have floating or adjustable interest rates.

### Item 1405: Allowance for Credit Losses

Item 1405 streamlines a number of the summary of loan loss experience disclosures currently required by Item IV of Guide 3, retains but updates the existing ratio of net charge-offs to average loans outstanding under Guide 3 and adds three additional credit ratios related to allowances for credit losses.

For each reported period, a registrant must disclose the following credit ratios, along with each component of the ratio's calculations:

- (1) allowance for credit losses to total loans outstanding at each period end;
- (2) nonaccrual loans to total loans outstanding at each period end;
- (3) allowance for credit losses to nonaccrual loans at each period end; and
- (4) net charge-offs during the period to average loans outstanding during the period.

The ratio for loan category for which disclosure is required in the financial statements is required to be disclosed. The registrant must provide a discussion of the factors that led to material changes in the above ratios or their related components for the periods presented.

Item 1405 codifies the requirement to provide a tabular allocation of the allowance disclosures based on the loan categories presented in the registrants' US GAAP financial statements for GAAP filers. This requirement does not apply to IFRS registrants, because IFRS already requires this disaggregated information in the financial statements.

## Item 1406: Deposits

Item 1406 codifies a majority of the deposit disclosures currently required by Item V of Guide 3, with some revisions.

For each reported period, a registrant must present separately the average amount of, and the average rate paid on, each of the following deposit categories that are in excess of 10 percent of average total deposits:

- (1) Non-interest-bearing demand deposits;
- (2) Interest-bearing demand deposits;
- (3) Savings deposits;
- (4) Time deposits; and
- (5) Other.

Additional categories that describe the nature of the deposits can be used if the registrant believes them to be more appropriate. If material, the registrant must present separately domestic deposits and foreign deposits for the amounts reported for the above categories. If material, the registrant also must disclose separately the aggregate amount of deposits by foreign depositors in domestic offices, without identifying the nationality of the depositors.

As of the end of each reported period, the registrant must present separately the amount of uninsured deposits.

Also, as of the end of the latest reported period, the registrant must state the amount outstanding of the portion of U.S. time deposits, by account, in excess of the Federal Deposit Insurance Corporation insurance limit or similar state deposit insurance scheme and time deposits that are otherwise uninsured by time remaining until maturity of (1) 3 months or less; (2) over 3 through 6 months; (3) over 6 through 12 months; and (4) over 12 months.

## Elimination of Certain Guide 3 Disclosures Regarding Return on Equity and Assets and Short-Term Borrowings

### RETURN ON EQUITY AND ASSETS

The rules do *not* codify Item VI of Guide 3, which calls for the the following ratios: return on assets, return on equity, dividend payout and equity to assets ratios.

The SEC stated that these ratios, though useful to investors, are not unique to bank and savings and loan registrants, which are the subject of Subpart 1400. Moreover, these ratios may be considered key performance indicators for registrants in general, which, if material to investors and used by management, should be identified and discussed as key performance indicators in a company's MD&A.

### SHORT-TERM BORROWINGS

The rules do *not* codify Item VII of Guide 3, except to the extent already provided in Item 1402 above with respect to the average balance and related average rate paid for each major category of interest-bearing liability disclosures.

The SEC believes that other elements currently called for by Item VII of Guide 3 are already covered by existing SEC rules and financial statement requirements.

### OTHER GUIDE 3 DISCLOSURE ITEMS NOT CODIFIED

In addition to the above, the final rules do not codify other Guide 3 disclosure items, including book value information, the maturity analysis of book value information and the disclosures related to investments exceeding 10 percent of stockholders' equity called for by Item II of Guide 3; loan category disclosure, the loan portfolio risk elements disclosure and the other interest-bearing assets disclosure called for by Item III of Guide 3; the analysis of loss experience disclosure called for by Item IV.A of

Guide 3; and the breakdown of the allowance disclosures called for by Item IV.B of Guide 3 for IFRS registrants.

## Related Amendments

The SEC also amended Article 9 of Regulation S-X, which applies to the consolidated financial statements filed for BHCs and to financial statements of banks that are included in SEC filings. Article 9 of Regulation S-X was amended to apply not only to BHCs and banks, but also to savings and loan associations and to savings and loan holding companies. This aligns the scope of Article 9 of Regulation S-X with the proposed scope of entities covered by Subpart 1400.

Item 9-03 of Article 9 of Regulation S-X, Item 404 of Regulation S-K, and certain instructions found in Form 20-F, were amended such that the references therein to Industry Guide 3 would now be changed to references to the new Subpart 1400.

## Practical Considerations

The final rules must be applied for the first fiscal year ending on and after December 15, 2021. A registrant that is filing an initial registration statement is not required to apply the final rules until an initial registration statement is first filed containing financial statements for a period on or after the mandatory compliance date.

Voluntary early compliance is permitted in advance of the mandatory compliance date, provided that the final rules are applied in their entirety from the date of early compliance.

In the SEC's economic analysis included in the adopting release, the SEC notes that affected entities likely will experience a decline in compliance costs as a result of the removal of overlapping disclosure items and reduced reporting periods. However, the adopting release notes that the reduction may be offset by an increase in costs associated with complying with the three new credit ratio disclosure

requirements and the additional disaggregated disclosure requirements.

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## Endnotes

- <sup>1</sup> Release No. 33-10835 (Sept. 11, 2020) (the "Release"), available at: <https://www.sec.gov/rules/final/2020/33-10835.pdf>.
- <sup>2</sup> The existing Securities Act Industry Guide 3 and Securities Exchange Act Industry Guide 3 are available at: <http://bit.ly/2kT1C3f>.
- <sup>3</sup> Release No. 33-5735 (Aug. 31, 1976), 41 FR 39007.
- <sup>4</sup> Release No. 33-10321 (Mar. 1, 2017), available at: <http://bit.ly/2l6nV5w> ("March 2017 RFP"). The March 2017 RFP

follows a concept release issued by the SEC in April 2016 that sought public comment on modernizing certain business and financial disclosure requirements in Regulation S-K, including whether the Industry Guides should be updated or codified into Regulation S-K. See Release No. 33-10064 (Apr. 13, 2016), available at: <http://bit.ly/2m7QEqT>.