

the abbreviated financial statements contain quantitative detail and related explanatory information regarding amounts included in the financial statements. Detailed quantitative disclosures and related explanatory material regarding many off-balance sheet items also would be omitted. For example, disclosure enumerating the composition of inventories and fixed assets, the terms and conditions of borrowings, the components of income tax expense and related deferred taxes, the status of pension fund assets and obligations, the assets and operating results of business and geographic segments, the details of restructuring charges and the characteristics of on-balance sheet and off-balance sheet financial instruments (including derivative instruments), among other things, would be omitted.

Other approaches for streamlining the annual report to shareholders include the concept of a summary annual report, the subject of a 1983 research study prepared for the Financial Executives Research Foundation ("FERF").¹³ The summary annual report concept is discussed in this release, and comments are solicited on the approach. Comment is also being solicited as to whether the Commission should allow registrants total flexibility, subject to the requirements of state corporate law and trading market listing agreements, by rescinding the proxy requirements regarding delivery of the annual report to shareholders.

Similar concerns about the complexity and volume of financial information, particularly in the notes to the financial statements, as well as the use of the annual report to shareholders in the integrated disclosure system, underlie additional rule proposals that would allow the use of abbreviated financial statements in the full spectrum of other disclosure documents required to be delivered to investors, such as prospectuses and transactional proxy statements.¹⁴ Use of abbreviated

financial statements in these circumstances raises additional issues, including the extent to which those making investment decisions would be willing to rely on the abbreviated financial statements and the practicality of requiring delivery of full financial statements upon request in various transactional contexts. A number of Commission registration forms, most notably Forms S-3 and F-3, already use a model of incorporation by reference, and delivery of incorporated documents upon request. The Commission invites comment as to the appropriateness and utility of such approach for both investors and issuers generally, and specifically with respect to each class of disclosure document covered by the proposed rulemaking.

The Commission recognizes that the feasibility of this initiative requires the confidence of registrants that they will not be subject to liability for failure to deliver the full financial statements in the annual report or other mandated disclosure documents. The rules proposed today include a safe harbor from liability for non-delivery of the note disclosures allowed to be excluded from the abbreviated financial statements. The proposals would not change the disclosure currently required outside the company's financial statements in mandated disclosure documents.

This initiative is part of the Commission's overall efforts to improve the effectiveness and efficiency of its disclosure system.¹⁵ Both the Commission and the Financial Accounting Standards Board ("FASB") recognize that an important part of that effort is to evaluate current financial disclosures to assess their continued utility and cost effectiveness.¹⁶

deliver abbreviated financial statements of that entity to investors, provided that the eligibility criteria are met.

¹⁵ See, e.g., Securities Act Release No. 7053 (April 19, 1994) [59 FR 21644] and Securities Act Release Nos. 7117, 7118 and 7119 (December 1, 1994) [59 FR 65628, 65632, and 65637] adopting amendments to Form 20-F and Regulation S-X [17 CFR 210] designed to streamline the financial information and reconciliation requirements for both foreign and domestic companies.

¹⁶ In response to the Financial Accounting Standards Advisory Council's 1994 Annual FASB Agenda Survey, survey respondents selected "Comprehensive Review of Financial Statement Disclosures" from a list of projects not currently on FASB's agenda and indicated that it should be given high priority by FASB. While FASB has not yet added a formal project to its agenda, the Chairman of FASB has indicated that FASB will be devoting significant resources to this issue. See Beresford, Dennis R. and Hepp, John A., *Financial Accounting Series: Status Report*, No. 149-B, "Financial Statement Disclosures: Too Many or Too Few?" at 7 (May 25, 1995).

II. Proposed Amendments To Permit Use of Abbreviated Financial Statements

A. Content of Abbreviated Financial Statements

The proposed rule amendments would permit eligible registrants to use abbreviated financial statements in specified disclosure documents delivered to shareholders and investors. The content of the abbreviated financial statements is set forth in proposed new Item 305(b) of Regulations S-K and S-B.¹⁷

The face of the abbreviated financial statements would have to include a prominent statement identifying them as such.¹⁸ Abbreviated financial statements would include balance sheets, statements of income and cash flows, and statements of changes in stockholders' equity that conform with GAAP and Regulation S-X with respect to classifications, measurements and periods presented.¹⁹ The notes to the abbreviated financial statements would be limited to the items specified in proposed Item 305.²⁰

¹⁷ Proposed Item 305 of Regulations S-B and S-K. References throughout the release to provisions of proposed Item 305 of Regulation S-K should be read to include the comparable provisions in proposed Item 305 of Regulation S-B. The two items are identical in all substantive respects, except that all but one of the references to Regulation S-X in proposed Item 305 of Regulation S-K are omitted from proposed Item 305 of Regulation S-B or changed to refer to Item 310 of Regulation S-B [17 CFR 228.310] (there is a reference to Article 2 of Regulation S-X [17 CFR 210.2] regarding accountants' reports in both the proposed Regulation S-K and S-B Items).

¹⁸ Proposed Item 305(b)(1) of Regulation S-K.

¹⁹ Proposed Items 305(b)(1) and (2) of Regulation S-K. Updating requirements for the abbreviated financial statements in prospectuses and proxy statements would be consistent with the updating requirements for the full financial statements. Accordingly, domestic issuers would follow the requirements of Rule 3-12 of Regulation S-X [17 CFR 210.3-12], while foreign issuers would follow the requirements of Rule 3-19 of Regulation S-X [17 CFR 210.3-19]. See proposed Regulation S-K Items 305(c) and (f)(2). Pursuant to proposed Regulation S-B Item 305(c), small business issuers would update their abbreviated financial statements in accordance with Item 310(d) of Regulation S-B [17 CFR 228.310(d)].

²⁰ The abbreviated financial statement proposals do not affect other disclosure requirements, such as the registrant's description of business, legal proceedings discussions, supplementary financial information, or Management's Discussion & Analysis ("MD&A") (Items 101, 103, 302, and 303 of Regulations S-B and S-K [17 CFR 228.101, 103, 302 and 303 and 229.101, 103, 302 and 303]). Registrants that currently cross-reference, but do not reiterate, data set forth in the notes to the financial statements in the MD&A section of their disclosure documents could not cross-reference notes omitted from the abbreviated financial statements. It is the current practice of many registrants to include supplementary financial information pursuant to Item 302 of Regulations S-K and S-B in an unaudited note to the financial

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¹³ "Summary Reporting of Financial Information—Moving Toward More Readable Annual Reports," Deloitte, Haskins & Sells (1983) ("FERF Report").

¹⁴ These documents include: (1) prospectuses required to be delivered in connection with offerings of securities pursuant to the Securities Act; (2) proxy or information statements required to be furnished pursuant to Section 14 of the Exchange Act [15 U.S.C. 78n]; (3) documents furnished to investors in connection with tender offers or going private transactions; (4) offering circulars delivered in connection with Regulation A [17 CFR 230.251-263] offerings; and (5) disclosure required to be furnished in connection with Regulation D offerings. If the disclosure document is required to include financial statements of another entity, such as an acquired business, significant subsidiary, or guarantor, the registrant also could choose to