

SEC Simplifies Some Disclosure Requirements for Public Companies

April 4, 2019

On March 20, 2019, the SEC adopted a collection of amendments to its rules and forms intended to modernize and simplify some of the disclosure requirements applicable to U.S. public companies.¹ The amendments implement a statutory directive under the 2015 FAST Act. They span a number of topics, including MD&A, property, risk factors, confidential treatment requests and exhibits.

Almost all of the changes remove or lighten previous requirements and many will be quite helpful for companies in practice. Therefore, a careful review of the revised form requirements in connection with upcoming filings is likely to prove worthwhile.

We discuss the more significant of the amendments below and summarize other, more ministerial amendments in a list at the end. Underlying the more significant changes is a principles-based approach that allows a company to tailor disclosure to its own circumstances and to make judgments about materiality, exemplifying a regulatory trend that can benefit companies and investors alike if it reduces irrelevant and immaterial disclosure.

The amendments relating to the redaction of confidential information in certain exhibits became effective immediately upon publication of the final rule release in the Federal Register on April 2, 2019. The rest of the amendments will become effective on May 2, 2019, except that a few (related to data tagging and some investment company filings) have longer phase-in periods. This means that calendar-year end companies can take advantage of the scaled back disclosure requirements in their 10-Qs covering the quarter ended March 31, 2019. The SEC staff has informally indicated that it will provide a mechanism for registrants to submit questions on the new rules and they could provide guidance that there may be no objection if companies filing their Forms 10-Q or 20-F prior to May 2, 2019 took advantage of the amendments.

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¹ Release No. 33-10618 (Mar. 20, 2019), available at <https://www.sec.gov/rules/final/2019/33-10618.pdf>.
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The following are the most significant amendments:

- Limitation of the requirement to provide year-to-year comparisons in MD&A to the two most recent fiscal years
- Elimination of the requirement to submit a confidential treatment request to the SEC for the redaction of confidential material in certain exhibits
- Inclusion of a description of all registered securities as an annual report exhibit
- Elimination, for all but new registrants, of the requirement to file material agreements entered into during the prior two years that are no longer in effect
- Ability to omit from all exhibits any schedules and similar attachments that do not contain material information
- Elimination of certain prescriptive line-item disclosure requirements for property disclosure and offering-related risk factors

Market participants have for many years been calling for a reexamination of the U.S. disclosure framework, which has built up by accretion as rules are added but rarely revised or removed. Disclosure overload is a widely recognized problem, and the build-up of prescriptive rules has certainly contributed to it, although other important factors include liability risk for “gatekeepers” like underwriters, officers, directors and auditors, and disclosure intended to address investor expectations. The complexity of the disclosure system is often cited as a deterrent to going (or remaining) public, and many have called for changes in the hope of encouraging IPOs.

The amendments were proposed on October 11, 2017² and were based in large part on the SEC staff’s November 2016 Report on Modernization and Simplification of Regulation S-K,³ as well as a July 2016 concept release on the business and financial disclosure requirements in Regulation S-K.⁴ They are part of a broader “disclosure effectiveness” initiative undertaken by the SEC and its staff, partly at the direction of Congress.⁵ However, the amendments do not tackle other areas where overly prescriptive disclosure has been most problematic, such as compensation disclosure or certain financial statement footnotes. We hope future proposals will include these items and perhaps even more comprehensive changes that not only roll back existing requirements but produce thoughtfully revised rules that contribute to more useful and less burdensome disclosure.

² Release No. 33-10425 (Oct. 11, 2017), available at <https://www.sec.gov/rules/proposed/2017/33-10425.pdf>.

³ Report on Modernization and Simplification of Regulation S-K (Nov. 23, 2016), which was mandated by the 2015 Fixing America’s Surface Transportation Act, available at <https://www.sec.gov/reportspubs/sec-fast-act-report-2016.pdf>.

⁴ See Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064 (Apr. 13, 2016), available at <https://www.sec.gov/rules/concept/2016/33-10064.pdf>.

⁵ See e.g., Disclosure Update and Simplification, Release No. 33-10532 (Aug. 17, 2018), <https://www.sec.gov/rules/final/2018/33-10532.pdf>; Modernization of Property Disclosures for Mining Registrants, Release No. 33-10570 (Oct. 31, 2018), <https://www.sec.gov/rules/final/2018/33-10570.pdf>; Request for Comment on Possible Changes to Industry Guide 3 (Statistical Disclosure by Bank Holding Companies), Release No. 33-10321 (Mar. 1, 2017), <https://www.sec.gov/rules/other/2017/33-10321.pdf>; and Request for Comment on Subpart 400 of Regulation S-K Disclosure Requirements Relating to Management, Certain Security Holders and Corporate Governance Matters, Release No. 33-10198 (Aug. 25, 2016), <https://www.sec.gov/rules/other/2016/33-10198.pdf>.

Year-to-Year Comparisons in Management's Discussion and Analysis

In an annual report on Form 10-K or Form 20-F, a company has historically been required to address the three-year period covered by the financial statements included in the filing, and to use “year-to-year comparisons or any other formats that in the registrant’s judgment would enhance a reader’s understanding.” Most companies provide year-to-year comparisons and do not use alternative formats. The discussion comparing the two earlier years is often repeated with minimal change from the previous year’s annual report.

The MD&A instructions will be revised to emphasize that a company may use any presentation that in its judgment enhances the reader’s understanding of the company’s financial condition, changes in financial condition and results of operations, without suggesting that any one mode of presentation is preferable to another.

The amendments also revise the instructions to the MD&A requirements to let a company omit a comparison with the earliest of the three years, if that comparison is included in a previous report or prospectus. A company that takes this approach must identify the location in the prior filing where the discussion may be found, but this does not require incorporating the prior filing by reference.

Lastly, the amendments eliminate language, currently in an instruction, regarding the potential need to reference the five-year selected financial data in the discussion of trends.

We expect that most companies will take advantage of the revised instructions to limit detailed MD&A comparisons to two years. A company taking this approach may also need to adjust MD&A disclosure about material known trends, if the earliest year (or a longer period) is

still relevant. In some cases, omitting any discussion of earlier periods might leave a gap in information. For example, revisions to the earliest year information as a result of a restatement or the retrospective adoption of a new accounting principle might be sufficiently material to warrant discussion. Ideally, companies would take the opportunity to craft improved MD&A disclosure that highlights material trends and year-to-year changes rather than simply walking through a list of changes in financial statement line items, but we do not expect to see significant changes to MD&A presentation, at least in the short term.

Materiality Thresholds for Risk Factors and Description of Property

Risk Factors

The requirement to disclose risk factors was originally applicable to offerings of securities, and it was extended to periodic reports in 2005. The amendments move the risk factor requirement from the section of Regulation S-K governing offerings to the one covering business-related information more generally (from Item 503 to a new Item 105 of Regulation S-K), and they remove a list of examples that were poorly adapted to periodic reports and inconsistent with the SEC’s principles-based approach to risk factor disclosures.

The Release emphasizes that the SEC seeks to discourage boilerplate risk factors and to encourage each company to focus on its own risk identification processes. Eliminating the list of examples is a small step to that end.

Description of Property

Under Item 102 of Regulation S-K, a company is required to disclose the location and general character of its “materially important physical properties” including those of its subsidiaries.

The revised rules provide that disclosure is only required “to the extent material,” and they eliminate from Item 102 a mixture of different disclosure triggers that the SEC believes have contributed to the disclosure of immaterial information. The revised instructions also specifically provide that disclosure can be provided on a collective basis, which could permit meaningful disclosure based on types of properties, geography or age of properties, among others.

Exhibits – Redacting Confidential Information

The amendments substantially simplify the process for seeking confidential treatment for information in a material contract or a plan of acquisition, reorganization, arrangement, liquidation or succession exhibit filed pursuant to paragraphs (b)(10) and (b)(2), respectively, of Item 601 of Regulation S-K, the Instructions to Exhibits in Form 20-F and Item 1.01 of Form 8-K. Securities Act Rule 406 and Exchange Act Rule 24b-2 would otherwise require a company to submit a confidential treatment request to the SEC explaining both why the information is immaterial and why public disclosure of the information will cause competitive harm to the company.

The amended rules eliminate the need for a confidential treatment request with respect to such exhibits. If the information is not material and disclosure would likely cause competitive harm to the company, the company may omit the information. It must mark the exhibit index to indicate that portions of the exhibit have been omitted, provide a prominent statement that portions have been omitted and indicate the location of the redactions. In contrast to the procedure under current rules, the revised rules do

not require a company to submit an unredacted version of the exhibit to the SEC at the time of filing with a confidential treatment request including an analysis of materiality and competitive harm associated with the redacted information. Instead, the SEC staff announced⁶ that it intends to selectively review filings with redactions and may, using a separate chain of comments from the regular comment process to minimize the risk of inadvertent public disclosure of competitive information, request that a company provide an unredacted version and a materiality and competitive harm analysis. Consistent with historical practice, the SEC staff will ask companies to resolve any questions relating to redacted exhibits in registration statements before submitting a request for acceleration of the effective date.

These amendments should be a welcome change for companies. Confidential treatment requests have become quite lengthy and time-consuming, and they are often done under time pressure to meet a Form 8-K deadline. The amendments do not, however, eliminate the need to analyze materiality and competitive harm.

Exhibits – Redacting Personal Information

The amendments permit a company to redact personal confidential information if disclosure would constitute “a clearly unwarranted invasion of personal privacy.” The SEC staff has informally permitted this for some time. These redactions will not require any further justification regarding materiality or competitive harm.

⁶ See <https://www.sec.gov/corpfin/announcement/new-rules-and-procedures-exhibits-containing-immaterial>, including a venue for transition questions: RedactedExhibits@sec.gov.

Exhibits – Adding Description of Registered Securities

Item 202 of Regulation S-K and Item 12 of Form 20-F require a registration statement to describe in detail the terms of the securities being offered.

The revised rules add an exhibit requirement to Item 601 of Regulation S-K for a company to provide this description, as an exhibit to its annual report,⁷ for all securities registered under Section 12 of the Exchange Act.⁸ This is the only change that will impose a significant new disclosure requirement.

Companies should be able to use the disclosure from prior registration statements to draft the new exhibit and would be permitted to incorporate the exhibit by reference into future annual reports, so long as there has not been any change to the information required by Item 202 in the interim. For companies that have not filed recent registration statements with respect to longstanding registered securities, this disclosure would not have been provided for some time and updates to previous descriptions may be required.

Additionally, it is possible that a company may make non-material amendments to the rights and privileges of its security holders during the course of a year that do not require separate disclosure on Form 8-K. Under the new exhibit requirement, the company will be required to update the description of securities each year for both non-material and material changes.

Exhibits – Omitting Schedules

The amendments permit a company to omit schedules (or similar attachments) from an exhibit to a registration statement or report, unless they contain material information that is not otherwise

disclosed in the exhibit or in the registration statement or report. Current rules allow the omission of schedules in only one circumstance (a plan of acquisition, reorganization, arrangement, liquidation or succession).

A company will be required to include in the exhibit a list briefly identifying the contents of all omitted schedules, unless a list is already included within the exhibit in a manner that conveys the subject matter of the omitted schedules and attachments (for example, we believe a table of contents will meet this requirement). It will also be required to submit a copy of any omitted schedule to the SEC staff upon request.

This should be a welcome reduction in the cost and effort relating to required exhibits. A company will need to review any schedules and other attachments to be omitted for any information that could be material.

Exhibits – Look-Back Period for Material Contracts

Under Item 601 of Regulation S-K and the instructions to exhibits in Form 20-F, a company is required to file all material contracts not made in the ordinary course of business if (1) the contract will be performed at or after the filing of the report or (2) the contract was entered into less than two years prior to the filing. The second condition applies even if the contract has been fully performed or is otherwise no longer in effect. The revised rules limit the (frequently long) list of material agreements to those that remain to be performed at the time of the filing, except for newly reporting registrants.

⁷ The SEC also adopted comparable revised language to the Instructions to Exhibits in Form 20-F.

⁸ Such securities consist of widely-held equity securities and debt securities listed on a national securities exchange.

Other Adopted Amendments

- Directors, Executive Officers, Promoters, and Control Persons (Item 401)
 - To clarify that the existing instruction permitting a company that provides information about its executive officers in its Form 10-K not to have to repeat that information in its proxy statement applies to all disclosure about executive officers required by Item 401 and not only Item 401(b) disclosure
- Compliance with Section 16(a) of the Exchange Act (Item 405)
 - To permit companies to rely only on electronically filed Section 16(a) reports to disclose whether any Section 16 filers missed or were not timely in their filings
 - To eliminate the requirement in Exchange Act Rule 16a-3(e) that reporting persons furnish copies of their electronically filed Section 16 reports to the registrant
 - To eliminate checkbox on cover page of Form 10-K that disclosure of delinquent Section 16 filings is not included
 - To add an instruction that no disclosure at all is required (even the heading) if there are no delinquencies to report, and to change the heading to “Delinquent Section 16(a) Reports”
- Corporate Governance (Item 407)
 - To update a reference to an outdated audit standard and to clarify that emerging growth companies are not required to disclose Compensation Discussion and Analysis
- Outside Front Cover Page of the Prospectus (Item 501(b))
 - To eliminate instructions that suggest a company should change its name if the name is too similar to that of a well-known company (but noting that the SEC staff may comment on potential name confusion)
 - To permit companies to include a statement that the offering price will be determined by another method as further explained in the relevant prospectus
 - To expand the required list of markets for the securities being offered to include all principal U.S. markets, not only national securities exchanges
 - To eliminate portions of legend requirements regarding compliance with state law offering requirements if state law is preempted
- Plan of Distribution (Item 508)
 - To define the term “sub-underwriter” in Securities Act Rule 405, which requires among other things disclosure about additional discounts and commissions paid to dealers acting as sub-underwriters
- Undertakings (Item 512)
 - To eliminate the requirement to include the undertakings in Regulation S-K Items 512(c), (d), (e) and (f) because they are obsolete or duplicative of other required filings

- Incorporation by Reference – Item 10(d)
 - To eliminate the prohibition on incorporating documents by reference generally if they have been on file with the Commission for more than five years
- Incorporation by Reference – Securities Act Rule 411, Exchange Act Rule 12b-23 and Rule 12b-32
 - To eliminate certain requirements to file copies of any information incorporated by reference as an exhibit (while retaining the requirement to file annual reports to security holders when incorporated by reference)
 - To require hyperlinks to information that is incorporated by reference if available on EDGAR
 - To generally prohibit incorporation by reference or cross-referencing in financial statements of information outside the financial statements
 - To restrict the incorporation of financial information required to be given in comparative form for two or more fiscal years or periods unless the information incorporated by reference includes the entire comparative period
 - To eliminate requirements that financial information incorporated by reference must comply with the requirements of the form or report into which it is incorporated
- XBRL Requirements
 - To require cover page data on many reports to be tagged in Inline XBRL
 - To include and tag the trading symbol for each class of registered securities on the cover page of Forms 10-K, 10-Q, 8-K, 20-F and 40-F

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