

SEC adopts rules to modernize and simplify disclosure

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Abstract

Purpose – To describe the modernization and simplification amendments of certain disclosure requirements of Regulation S-K and related rules and forms recently adopted by the US Securities and Exchange Commission (SEC).

Design/methodology/approach – This article provides an overview of the amendments, their effective dates and related practical considerations for companies.

Findings – The amendments cover many provisions within Regulation S-K and affect various forms that rely on the integrated disclosure requirements of Regulation S-K. The amendments are designed to enhance the readability and navigability of SEC filings, to discourage repetition and disclosure of immaterial information and to reduce the burdens on registrants, all while still providing material information to investors. The amendments contain several changes relating to confidential information contained in exhibits. For consistency, parallel amendments have been adopted to rules other than Regulation S-K, as well as to forms for registration statements and reports.

Practical implications – Most of the amendments are effective May 2, 2019. The amendments relating to the redaction of confidential information in certain exhibits became effective April 2, 2019. Given these dates, companies should review the rule changes implemented by the amendment now and consider how they will impact their disclosure in upcoming SEC filings.

Originality/value – Practical guidance from experienced lawyers in the Corporate & Securities practice.

Keywords Disclosure, Confidentiality, US Securities and Exchange Commission (SEC), Management's discussion and analysis (MD&A), SEC Regulation S-K

Paper type Technical paper

On March 20, 2019, the US Securities and Exchange Commission (SEC) adopted amendments intended to modernize and simplify certain disclosure requirements of Regulation S-K and related rules and forms^[1]. The amendments represent the next step in a series the SEC has taken to update and modernize the disclosure requirements in Regulation S-K. For example, in August 2018, the SEC adopted disclosure update and simplification amendments that became effective in November 2018^[2]. We anticipate the SEC will continue to address other pending changes to Regulation S-K in the near future.

The amendments were adopted pursuant to the Fixing America's Surface Transportation Act (FAST Act). The FAST Act required the SEC to prepare a report on modernizing and simplifying the disclosure requirements of Regulation S-K and related rules and forms, which the SEC Staff completed in November 2016^[3]. In October 2017, the SEC issued a proposal to implement the recommendations in that report. According to the SEC's adopting release, these amendments "are intended to improve the quality and accessibility of disclosure in filings by simplifying and modernizing" SEC requirements, consistent with the FAST Act.

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Overview of the amendments

The amendments cover many provisions within Regulation S-K and affect various forms that rely on the integrated disclosure requirements of Regulation S-K. The amendments are designed to enhance the readability and navigability of SEC filings, to discourage repetition and disclosure of immaterial information and to reduce the burdens on registrants, all while still providing material information to investors. Many of the amendments are technical in nature. Some amendments eliminate redundant or obsolete requirements or streamline the applicable rules. For consistency, parallel amendments have been adopted to rules other than Regulation S-K, as well as to forms for registration statements and reports. Some amendments are designed to streamline or otherwise improve disclosure requirements, while others update rules to reflect developments since their adoption or last amendment. In some cases, the amendments require additional disclosure or use of technology. This article discusses highlights of the amendments.

MD&A

The pre-amendment instructions for management's discussion and analysis of financial condition and results of operations (MD&A), set forth in Item 303(a) of Regulation S-K, generally specify that discussion of the three-year period covered by the financial statements shall either use year-to-year comparisons or other formats that, in the registrant's judgment, would enhance a reader's understanding of a company's financial condition, changes in financial condition and results of operations. These instructions also state that where trend information is relevant, reference to five-year selected data may be necessary.

The amendments eliminate the reference to year-to-year comparisons in the instructions to Item 303(a). The revised instructions provide that a registrant may use any presentation that in its judgment enhances a reader's understanding of the registrant's financial condition, changes in financial condition and results of operations, but does not suggest that any one mode of presentation is preferable to another. The amendments to the Item 303(a) instructions also eliminate the need to discuss the earliest year in certain circumstances if financial statements included in a filing cover three years. As amended, the discussion of the earliest year is not required in MD&A if discussion was already included in the registrant's prior filings on the SEC's Electronic Data Gathering and Retrieval (EDGAR) system, provided that the registrant identifies the location in the prior filing where the omitted discussion may be found.

The elimination of the earliest (i.e. the third) year discussion in the MD&A does not impact smaller reporting companies (SRCs) or emerging growth companies (EGCs). The amendments do not change the existing rule allowing SRCs to limit their MD&A to the two-year period covered by their financial statements. Nor does it change the ability of EGCs to limit their MD&A to audited periods presented in the financial statements when the EGCs provided two years of audited financial statements in an initial public offering.

The MD&A amendments eliminate the reference to discussion of the five-year selected financial data being needed when trend information is important. Trend information is already required for a number of parts of MD&A, including liquidity and capital resources and results of operations. Eliminating the requirement to also show five years of selected financial information was intended to eliminate duplication and focus companies on providing the trend disclosure in the MD&A.

The amendments make conforming changes to the MD&A requirements for foreign private issuers contained in the instructions to Item 5 (Operating and Financial Review) of Form 20-F. However, because the MD&A contained in Form 40-F, which is used by Canadian issuers, is prepared in accordance with applicable Canadian requirements, there are no corresponding revisions to that form.

Confidential portions of exhibits

The SEC made several changes to Item 601 of Regulation S-K relating to confidential information contained in exhibits that are designed to streamline the confidential treatment process. The amendments revise Item 601(b)(10) to permit registrants to omit confidential information from material contracts filed as exhibits without submitting a confidential treatment request (CTR) to the SEC if such information is both not material and would likely cause competitive harm if disclosed. A similar amendment was made to Item 601(b)(2) to allow redaction of immaterial provisions or terms in agreements relating to acquisitions, reorganizations, arrangements, liquidations or successions that would likely cause competitive harm if publicly disclosed. The SEC also expanded this type of redaction to certain exhibit-related requirements in specified disclosure forms for which Item 601(b)(10) does not apply, such as Form 20-F. In addition, the amendments also made conforming changes to Item 1.01 of Form 8-K with respect to material contracts filed with that form.

When relying on these provisions, registrants must:

- limit the redacted information to no more than necessary to prevent competitive harm;
- mark the exhibit index to indicate that portions have been omitted;
- include a prominent statement on the first page of each redacted exhibit indicating that information in the marked sections of the exhibit has been omitted because it is both not material and would likely cause competitive harm to the company if publicly disclosed; and
- indicate with brackets where the information has been omitted from the filed version of the exhibit.

In addition, upon request of the SEC Staff, registrants are required to provide supplemental materials to the SEC Staff, including both an unredacted paper copy of the exhibit in question and an analysis of why the redacted information satisfies the test for non-disclosure. Companies would be able to continue to use Rule 83 to request confidential treatment of supplemental information provided to the SEC Staff.

If a company has a CTR pending on the effective date for the amended rules covering redaction of confidential information in material contracts, it may, but is not required to, withdraw its application. The adopting release advises companies that opt to withdraw a pending request in such circumstances to refile redacted exhibits in accordance with the amendments.

In addition, the SEC added a new paragraph (a)(5) of Item 601 of Regulation S-K to allow registrants to omit entire schedules and similar attachments to exhibits unless they contain material information that is not otherwise disclosed in the exhibit or the disclosure document. A list briefly identifying the contents of omitted schedules must be contained in the exhibit and any omitted schedule would need to be submitted to the SEC Staff on a supplemental basis upon request. The existing provision contained in Item 601(b)(2) of Regulation S-K, which permitted only the omission of schedules and attachments relating to plans of acquisition, reorganization, arrangement, liquidation or succession, was deleted since the new paragraph (a)(5) now covers all exhibits filed under Item 601.

The SEC also added a new paragraph (a)(6) of Item 601 of Regulation S-K that allows registrants to omit personally identifiable information from exhibits without submitting a CTR.

Other exhibit amendments

Prior to the amendments, Item 601(b)(10) of Regulation S-K required material contracts to be filed not only when the contract must be performed in whole or in part at or after the filing of the registration statement or report but also when the contract was entered into not more

than two years before the filing. The amendments eliminate the two-year look-back for material contracts for all but newly reporting registrants. Investors will continue to have access to previously filed material contracts through EDGAR.

Item 601(b)(4)(vi) of Regulation S-K, setting forth exhibit requirements for instruments defining the rights of security holders, was amended to require registrants to provide an additional exhibit to Form 10-K containing the description required by Items 202(a)-(d) and (f) of Regulation S-K for each class of their securities that is registered under Section 12 of the Securities Exchange Act of 1934, as amended (Exchange Act). Previously, a description of securities had been required by Item 202 in registration statements, but not in Form 10-K or Form 10-Q. The new requirement does not change existing disclosure obligations under Form 8-K or Schedule 14A, which require registrants to disclose certain modifications to the rights of their security holders and amendments to their charter or bylaws, or the current requirement to file a complete copy of the amended charter or bylaws.

The amendments make conforming changes to the exhibit requirements for foreign private issuers in Form 20-F, which continues a long-standing attempt to conform the exhibit requirements for Form 20-F with the exhibit requirements for registration statements filed by domestic issuers. However, the SEC did not make similar changes to Form 40-F.

Property

The SEC has amended Item 102 of Regulation S-K to emphasize materiality by requiring disclosure of principal physical properties *to the extent material* to the registrant. These disclosures may be provided on a collective basis if appropriate. However, the amendments do not modify instructions to Item 102 that are specific to the oil and gas industry.

Section 16 disclosure

The amendments revise Item 405 of Regulation S-K to clarify that registrants may rely on Section 16 reports filed on EDGAR (as opposed to copies furnished to the registrant) to determine if there are any late filings. Also, the heading for such disclosure is changed to “Delinquent Section 16(a) Reports” instead of “Section 16(a) Beneficial Ownership Reporting Compliance.” An instruction encourages this caption to be excluded if there are no delinquencies to report. The amendments also eliminate the checkbox on the cover page of Form 10-K relating to late Section 16 filing disclosure.

Executive officer disclosure

The instructions to Item 401 of Regulation S-K have been revised to clarify that registrants do not need to duplicate executive officer disclosure under such item in their proxy statements if they have already provided it in Part I of their Form 10-K. The prior location of the applicable instruction in Item 401(b) created uncertainty as to whether it covered those executive officers disclosures required by the other paragraphs of Item 401. To reflect a “plain English” approach, the amendments change the caption for such disclosure to “Information about our Executive Officers”.

Registration statement/prospectus requirements

The amendments modify Item 501 of Regulation S-K so that if the offering price will be determined by a particular method or formula, the description of the method or formula may be omitted from the prospectus cover page and be more fully explained in the prospectus. This disclosure requires a cross-reference to the offering price method or formula

disclosure, including a page number that is highlighted by prominent type or in another manner.

Item 501 of Regulation S-K was amended to require the cover page of a prospectus to disclose the principal US markets for the securities being offered and their corresponding trading symbols rather than limiting such information to listings on a national securities exchange. The amendments limit disclosure relating to markets that are not national securities exchanges to those principal US markets where the registrant, through the engagement of a registered broker-dealer, had achieved quotation.

The amendments also permit registrants to exclude the portion of the “Subject to Completion” legend relating to state law if the offering is not prohibited by state blue sky law.

Risk factors

The SEC’s risk factor disclosure amendments reflect regulatory streamlining rather than any change in the principles-based requirement of risk factor disclosure. The amendments move the requirements for risk factor disclosure out of Item 503 of Regulation S-K into a new Item 105. The SEC eliminated the specific examples of risk factors from Regulation S-K to encourage registrants to focus on their own risk identification process.

Incorporation by reference

Rule 12b-23(b) under the Exchange Act, which addresses incorporation by reference, has been amended to prohibit financial statements from incorporating by reference, or cross-referencing, information that is contained outside of the financial statements unless otherwise specifically permitted or required by the SEC’s rules, US generally accepted accounting principles (US GAAP) or International Financial Reporting Standards, whichever is applicable. According to the SEC, such incorporation by reference from outside the financial statements can raise questions as to the scope of an auditor’s responsibilities. On the other hand, the SEC did not change the ability of registrants to cross-reference to or incorporate information from the financial statements to satisfy the narrative disclosure requirements of Regulation S-K.

The amendments eliminate provisions in Rule 12b-23 under the Exchange Act and Rule 411 of the Securities Act of 1933, as amended, that had required information incorporated by reference to have been filed as an exhibit, with limited exceptions. In addition, the amendments eliminate the requirement previously contained in Item 10(d) of Regulation S-K that generally prohibits registrants from incorporating documents by reference that have been on file with the SEC for more than five years.

Additional hyperlinks

Some of the disclosure modernization and simplification amendments require incorporation of technology developments. For example, the SEC already requires that the exhibit index of specified SEC filings be hyperlinked to the location of the relevant exhibit on EDGAR. The amendments expand the use of hyperlinking by requiring registrants to provide hyperlinks to information that is incorporated by reference, whether or not the information is in a document filed as an exhibit, if that information is available on EDGAR. Unlike the exhibit hyperlink requirement, a registrant is not required to correct inaccurate hyperlinks in an effective registration statement by including a corrected hyperlink in a subsequent periodic report or post-effective amendment.

Exchange act filings

To further enhance investors' ability to use interactive data, the amendments provide that information on the cover pages of Forms 10-K, 10-Q, 8-K, 20-F and 40-F will be required to be tagged in Inline XBRL, HTML format with embedded XBRL data, subject to a transition period described below. The Inline XBRL requirement is similar to a recent SEC rule change requiring Inline XBRL for operating company financial statements. In addition, the amendments require the cover pages of Forms 10-K, 10-Q, 8-K, 20-F and 40-F to include the trading symbol for each class of the registrant's registered securities.

Updating regulation S-K

The amendments eliminate a reference to an outdated auditing standard contained in Item 407(d) of Regulation S-K relating to audit committee discussions with independent auditors, replacing it with a general reference to the applicable requirements of the Public Company Accounting Oversight Board. The amendments also update Item 407(e) to specifically exclude EGCs from the requirement to provide a compensation committee report because they are not required to provide a compensation discussion and analysis. In addition, the SEC eliminated certain obsolete undertakings contained in Item 512 of Regulation S-K.

Effective date

Most of the amendments are effective May 2, 2019. However, the amendments relating to the redaction of confidential information in certain exhibits became effective April 2, 2019.

The requirements to tag data on the cover pages of certain filings are subject to a three-year phase-in. Large accelerated filers that prepare their financial statements in accordance with US GAAP will need to comply with this tagging requirement in reports for fiscal periods ending on or after June 15, 2019. Accelerated filers that prepare their financial statements in accordance with US GAAP will need to comply with this requirement for reports for fiscal periods ending on or after June 15, 2020. All other filers will need to comply for reports for fiscal periods ending on or after June 15, 2021.

All investment company registration statement and Form N-CSR filings made on or after April 1, 2020 must be made in HTML format and comply with the rule and form amendments pertaining to the use of hyperlinks.

Guidance

On April 1, 2019, the SEC Staff announced guidance with respect to the new rules and procedures for the filing of exhibits containing immaterial, competitively harmful information [4]. The SEC Staff indicated that it will separate requests for supplemental information related to redacted exhibits from its regular filing review comments. Companies should respond separately to any requests for supplemental information with respect to compliance with the new rules regarding redacted exhibits and follow the specific delivery instructions that the SEC Staff will provide when requesting such material.

Companies are permitted to request confidential treatment of supplemental materials while they are in the SEC's possession pursuant to Rule 83. The new rules did not change the rules for new or pending confidential treatment requests (CTR), which can continue to be made and will continue to be processed. Companies may withdraw a pending CTR in favor of reliance on the new rules for exhibit redaction. The Staff's guidance stated that in such situations a company *must* amend its filing to conform to the new rule requirements.

Practical considerations

Given how quickly the new requirements are coming into effect, companies should review the rule changes implemented by the amendment now and consider how they will impact their disclosure in upcoming SEC filings.

Some of the amendments are designed to encourage companies to take a “fresh look” at prior year disclosures and to focus on materiality. Companies should review their applicable disclosure controls and procedures in light of the amendments. This is particularly true for the changes to MD&A and risk factor disclosure rules.

The amendments did not modify the executive compensation disclosure requirements contained in Item 402 of Regulation S-K, which were the subject of a separate SEC comment request. The amendments did move Instruction 3 to Item 401(b) to make it a general instruction to Item 401 in order to clarify that disclosure about an issuer’s executive officers need not be duplicated in proxy statements if provided in Part 1 of Form 10-K.

Companies will need to include a new exhibit for their Form 10-K to provide a brief description of each class of their capital stock, debt securities, warrants, rights, American Depositary Receipts or other securities registered under the Exchange Act. While this information should already be available in other forms, for example, in a registration statement, companies should review that disclosure to determine if any information needs to be updated for their Form 10-K exhibit. Calendar-year companies may have plenty of time to assess the readiness of their prior disclosures for this new exhibit, but some non-calendar year companies may need to do this sooner. For issuers with many series of listed debt securities, these disclosures may be extensive. In future years, if any changes are made to the rights and privileges of a registrant’s securities, whether material or non-material, new Item 601(b)(4)(vi) will require the registrant to update the description of its securities for its next Form 10-K exhibit.

As a reminder, in August 2018 the SEC adopted disclosure update and simplification amendments that became effective on November 5, 2018, which was around the time that many companies were preparing quarterly reports on Form 10-Q. Those amendments contained a new requirement to present the changes in shareholders’ equity in the interim financial statements (either in a separate statement or footnote) in Form 10-Q. Because of the proximity of the effectiveness of those amendments to a Form 10-Q filing date, the SEC Staff issued temporary transitional relief from complying with that new requirement. Compliance and Disclosure Interpretation 105.09 stated that the staff would not object if a filer’s first presentation of the changes in shareholders’ equity is included in its Form 10-Q for the quarter that begins after November 5, 2018. Companies that have relied on this guidance need to be sure to include changes in shareholder’s equity in their upcoming reports on Form 10-Q.

Although the SEC encourages issuers to delete the caption for Section 16 delinquencies if there are none to be reported in a given year, registrants should consider whether this deletion may lead to inadvertent omissions of required disclosures in subsequent years.

Notes

1. Available at: www.sec.gov/rules/final/2019/33-10618.pdf
2. For further information see [Mayer Brown’s Legal Update \(2018a, 2018b\)](#)
3. See *Report on Modernization and Simplification of Regulation S-K* (Nov. 23, 2016), available at: www.sec.gov/reportspubs/sec-fast-act-report-2016.pdf
4. Available at: www.sec.gov/corpfin/announcement/new-rules-and-procedures-exhibits-containing-immaterial

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