
LEGAL UPDATES AND NEWS

SEC Adopts Changes to Its Disclosure Requirements for Periodic Reports and Registration Statements

The Securities and Exchange Commission (the “SEC”) recently adopted amendments to certain disclosure requirements for periodic reports and registration statements. These changes affect disclosure regarding the description of the registrant’s business, risk factors and legal proceedings.

These new amendments are the most recent action in the SEC’s disclosure modernization efforts. The particular provisions at issue have not been significantly revised for more than 30 years. The stated purposes for the proposed changes are to make disclosure more relevant to investors while reducing the burden on issuers. The changes eliminate certain prescriptive requirements in favor of a principles-based, company-specific approach, and permit an increased use of summaries, cross-references and hyperlinks to reduce repetition and discourage overly lengthy disclosure. The amendments will go into effect no earlier than mid-October 2020, 30 days after they are published in the Federal Register.

Description of Registrant’s Business

Item 101 of Regulation S-K, which sets forth the disclosure requirements for the Description of Business section that is provided in a registrant’s annual report on Form 10-K or in a registration statement, is being updated to shift from the prescriptive list of items for disclosure that is currently provided to a more “principles-based” disclosure regime that permits issuers to determine, in their judgment, what developments are material to an understanding of the business. The changes include the following:

- requiring new descriptions, where material to an understanding of the business, of (1) a registrant’s “human capital resources” and (2) “any human capital measures or objectives that the registrant focuses on in managing the business (such as, depending on the nature of the registrant’s business and workforce, measures or objectives that address the development, attraction and retention of personnel)”;
- requiring disclosure of material changes to a previously disclosed business strategy (without mandating that business strategies be disclosed) as a supplement to MD&A-related disclosure requirements;
- expanding regulatory compliance disclosure requirements to cover all material government regulations, not just environmental laws;
- updating the rules relating to the narrative description of a registrant’s business to refer to a non-exclusive list of disclosure topic examples, including, among other topics, revenue-generating activities, products and services, resources material to a registrant’s business (e.g., raw materials and intellectual property) and material effects of compliance with government regulations on capital expenditures, earnings and competitive position;
- eliminating the current five-year disclosure lookback (three years for smaller reporting companies); and

- permitting the business description to include only updates from previously filed information (rather than a full restatement), paired with a hyperlink to a single previously filed full discussion.

Furthermore, while the revised requirements of Item 101 move away from the old list of items for disclosure, it will still include a non-exhaustive list of disclosure topics that “may” be disclosed, including:

- revenue-generating activities, products or services, and any dependence on revenue-generating activities, key products, services, product families or customers, including government customers;
- status of development efforts for new or enhanced products, trends in market demand and competitive conditions;
- resources material to the business, such as sources and availability of raw materials and duration and effect of intellectual property;
- any material portion of the business subject to renegotiation or termination by the government; and
- seasonality.

Risk Factors

The new amendments include multiple changes to Item 105 of Regulation S-K, which sets forth the disclosure requirements for risk factors. The stated goal of these changes is to minimize “generic” or “boilerplate” risk factors in favor of a more tailored disclosure. These changes include the following:

- if the risk factor section exceeds 15 pages, the registrant must include a two-page summary of the risk factors using “concise, bulleted or numbered statements” in the forepart of the prospectus or annual report;
- the risk factors should be organized under relevant headings for groups of risk factors; and
- any generic risk factors should be included together at the end of the risk factor section under the caption “General Risk Factors.”

Legal Proceedings

The amendments to Item 103 of Regulation S-K will increase the quantitative threshold for disclosure of environmental proceedings to which the government is a party from \$100,000 to \$300,000, unless the registrant selects a different threshold. Any alternative threshold must be reasonably designed (as determined by the registrant) to result in disclosure of material environmental proceedings and may not exceed the lesser of \$1 million or one percent of the current assets of the registrant and its subsidiaries on a consolidated basis.

The new rules also permit the litigation disclosure to be included by cross referencing or hyperlink to another place in the document where the disclosure is made.

Items for Consideration

The amendments will go into effect 30 days after they are published in the Federal Register. As of the date of this newsletter, the amendments had not yet been published in the Federal Register, so the earliest the amendments could become effective would be mid-October 2020, which would make the changes applicable to quarterly reports filed for the quarter ended September 30th. With the current COVID-19

pandemic, the SEC has delayed the implementation of certain changes it intends to make to its disclosure regime. If publication of the amendments were to be delayed until mid-October 2020, then the changes would not be applicable for most registrants until their annual or quarterly reports, as applicable, for the period ended December 31st.

When thinking about how these amendments will change the disclosure provided in their periodic reports and registration statements, registrants should consider:

- evaluating their business disclosure and whether any changes should be made to their first filing due to the new principles-based approach (future filings will be able to incorporate by reference this disclosure and supplement it only with material developments);
- evaluating their business section and the new list of “optional” disclosures (some disclosure may no longer be needed due to the new principles-based approach, but new disclosures may be needed);
- adding human capital management information to their disclosures (if the business section does not already have such disclosure);
- organizing their risk factors under separate headings – e.g., business issues, asset quality factors, interest rate risk, economic and market area risks and offering issues (if risk factors are not already organized in such a manner);
- reviewing their risk factors to determine which describe generic risks that are broadly applicable to all companies and move these risk factors under a separate heading at the end of the risk factors section;
- evaluating their disclosure of environmental regulatory actions to determine whether this will result in reduced required disclosure; and
- updating their disclosure documents to take advantage of item that can be cross referenced or hyperlinked under the new rules.

* * * * *

Please contact any of our attorneys below if you have any questions regarding the information contained in this newsletter.

John Gorman	■ (202) 274-2001	jgorman@luselaw.com
Lawrence Spaccasi	■ (202) 274-2037	lspaccasi@luselaw.com
Kip Weissman	■ (202) 274-2029	kweissman@luselaw.com
Marc Levy	■ (202) 274-2009	mlevy@luselaw.com
Ned Quint	■ (202) 274-2007	nquint@luselaw.com
Benjamin Azoff	■ (202) 274-2010	bazoff@luselaw.com
Michael Brown	■ (202) 274-2003	mbrown@luselaw.com
Scott Brown	■ (202) 274-2013	sbrown@luselaw.com
Victor Cangelosi	■ (202) 274-2028	vcangelosi@luselaw.com
Jeffrey Cardone	■ (202) 274-2033	jcardone@luselaw.com
Thomas Hutton	■ (202) 274-2027	thutton@luselaw.com
Steven Lanter	■ (202) 274-2004	slanter@luselaw.com
Gary Lax	■ (202) 274-2031	glax@luselaw.com

© 2020 Luse Gorman, PC. Luse Gorman, PC is a Washington, DC-based law firm that specializes in representing domestic and foreign financial institutions in the United States. The information provided herein does not constitute legal advice and relates only to matters of federal law and not to any particular state law.