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LEGAL UPDATES AND NEWS

SEC Adopts Changes to MD&A and Financial Disclosure Rules

The Securities and Exchange Commission (the "SEC") recently adopted amendments to modernize, simplify and enhance certain financial disclosure provisions, including the Management's Discussion and Analysis ("MD&A") section.

These amendments are the most recent action in the SEC's disclosure modernization efforts. The amendments are intended to enhance the focus on material information for the benefit of investors, while simplifying compliance efforts for companies. The amendments are also intended to improve disclosure by enhancing its readability, discouraging repetition and eliminating immaterial information. Companies will not be required to comply with the new rules until July 2021, at the earliest, though early adoption will be allowed.

Elimination or Reduction of Certain Financial Disclosure Requirements

The amendments eliminate or reduce certain financial disclosure requirements, including those discussed below, to reduce duplication and focus on material information.

Selected Financial Data

The amendments eliminate the requirement for five years of selected financial data to be provided. However, in its adopting release, the SEC encouraged companies to consider whether trend information for periods earlier than those presented in the financial statements may be necessary to comply with the objectives of MD&A disclosure to "provide material information relevant to an assessment of the financial condition and results of operations." The SEC also suggested that companies consider whether the tabular presentation of relevant information as part of an introductory section or overview, including to demonstrate material trends, may help a reader's understanding of the MD&A.

Supplementary Financial Information

Companies will no longer be required to provide tabular disclosure of two years of selected quarterly financial data. Instead, companies will be required to provide tabular disclosure under this item only when there are material retrospective changes that pertain to the statements of comprehensive income for any of the quarters within the two most recent fiscal years and any subsequent interim period. If such disclosure is provided, companies will also be required to provide an explanation of the reasons for such material changes and to disclose, for each affected quarterly period and the fourth quarter in the affected year, summarized financial information related to the statements of comprehensive income and earnings per share reflecting such changes. Consistent with current standards, smaller reporting companies will not be required to provide information under this item.

Changes to MD&A Requirements

The amendments also include changes intended to modernize, simplify and enhance MD&A disclosure requirements, including the following significant changes.

Objective

The amendments include a description of the objective of MD&A, largely pulling from different requirements and instructions provided in the current rules. These amendments are generally intended to remind companies that MD&A should provide an analysis that encompasses both a historical and prospective analysis of a company's financial condition and results of operations. The SEC's adopting release places particular emphasis on providing analysis covering the company's prospects for the future.

Material Changes to Line Items

The amendments clarify that MD&A requires a narrative discussion of the "underlying reasons" for material changes from period to period in a line item in quantitative and qualitative terms, rather than only the "cause" for material changes. The amendments also clarify that companies should discuss material changes within a line item even when such material changes offset each other.

Liquidity and Capital Resources

The amendments specify that a company should broadly disclose material cash commitments, including capital expenditures. The current requirement is for companies to discuss their material commitments for capital expenditures as of the end of the latest fiscal period, and to indicate the general purpose of the commitments and the anticipated sources of funds to fulfill them. The new requirement calls for companies to describe their material cash requirements as of the latest fiscal period (including commitments for capital expenditures), the anticipated sources of funds to fulfill them and the general purpose of the cash requirements.

In light of this amended disclosure requirements and overlap with certain information required in the financial statements, the amendments eliminate the requirement to provide a contractual obligations table.

Off-Balance Sheet Arrangements

The current item requiring disclosure of off-balance sheet arrangements will be eliminated by the amendments and replaced with a general instruction that companies discuss commitments or obligations, including contingent obligations, that have, or are reasonably likely to have, a material effect on their financial condition, revenues or expenses, results of operations, liquidity, cash requirements or capital resources even when there is no obligation reported in the consolidated balance sheets. This change is intended to place any discussion of off-balance sheet arrangements in the broader context of the MD&A instead of in a separately captioned section with prescriptive requirements.

Critical Accounting Estimates

The amendments codify and provide clarification on existing SEC guidance regarding critical accounting estimates by explicitly requiring their disclosure. For each critical accounting estimate, the amendments require companies to disclose why the estimate is subject to uncertainty and, to the extent information is material and reasonably available, how much each estimate and/or assumption has changed during the relevant period, and the sensitivity of the reported amounts to the methods, assumptions and estimates underlying the estimate's calculation. Companies will also be required to provide quantitative as well as qualitative information necessary to understand uncertainty regarding the estimate and the impact the estimate has had or is reasonably likely to have on their financial condition or results of operations, to the extent the information is reasonably available and material. In the adopting release, the SEC noted that companies often repeat the information from the financial statement footnotes about significant accounting policies and that the amendments are intended to eliminate duplicative disclosures and, instead, promote enhanced analysis of measurement uncertainties to supplement the disclosure in the financial statements.

Interim Periods

The amendments provide flexibility in how companies can compare their results of operations for the most recently completed quarter. Companies will be able to compare their most recent results to either the corresponding quarter of the prior year (as currently required) or to the immediately preceding quarter. If a company switches the basis of its comparison, it must discuss the reasons for the change and provide both comparisons in the filing where the change is announced. While the amendments provide flexibility on the presentation of the quarterly comparisons, the current requirement to discuss any material changes in the results of operations between the most recent fiscal year-to-date interim period and the corresponding period in the preceding fiscal year remain unchanged.

Timing

The amendments will be effective 30 days after their publication in the Federal Register (the "Effective Date"). However, compliance with the amendments will not become mandatory for companies until their first fiscal year ending on or after the date that is 210 days after the amendments are published in the Federal Register (the "Mandatory Compliance Date"). This means that compliance with the amendments will not become mandatory until July 2021, at the earliest. Companies will be required to apply the amended rules in a registration statement and prospectus that on its initial filing date is required to contain financial statements for a period on or after the Mandatory Compliance Date. While companies will not be required to apply the amended rules until the Mandatory Compliance Date, they may comply with the amendments any time after the Effective Date, so long as they provide disclosure responsive to an amended item in its entirety.

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

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