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"DExit" and Disclosures – Atkins' Remarks on State Competition and Risk Factors

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Over the past few months, Cadwalader's *Quorum* has closely followed the remarks of U.S. Securities and Exchange Commission (SEC) Chairman Paul S. Atkins as they relate to the SEC's revitalized mandate to spur capital markets by prompting competition among the states and easing disclosure burdens. Atkins' February 17th speech at the Texas A&M School of Law Corporate Law Symposium at the Texas A&M School of Law Corporate Law Symposium focused on two areas: one, a familiar target, the state of Delaware, but the second addressed a new topic within Regulation S-K of the Securities Exchange Act, risk factor disclosure.

"DExit" and State Competition to Attract Incorporators

Atkins has consistently applied pressure on Delaware, specifically to reform the shareholder litigation landscape by permitting mandatory arbitration provisions for securities claims in an issuer's governing documents. While Atkins' previous remarks about state corporate law and its effects on public companies have centered on Delaware's supposed missteps, his February 17th speech endorses efforts recently taken by Texas to compete in the market for a corporation's jurisdiction of incorporation.

In his speech, Atkins highlighted a few steps Texas has taken to "further its appeal as a destination for corporate domestication," including limiting the ability of litigants to recover fees for actions that result in (or settle for) additional or amended disclosures only, and adopting a regime that permits a corporation to require lawsuits regarding internal affairs be exclusively brought in Texas courts and/or to waive trial by jury.

In addition to recognizing these changes, Atkins encouraged Texas to consider permitting mandatory arbitration provisions and instituting fee shifting models beyond those provided for in Rule 11 of the Federal Rules of Civil Procedure (for frivolous claims).

In bringing attention to "DExit" and Texas' push to attract corporations to its state, Atkins champions Texas as a state that is advancing a vision that is rooted in a "deeply American idea: that competition – among firms; among markets; and yes, among States – is the animating force behind a system that has produced more prosperity than any other in human history."

While some prominent companies have relocated to Texas (*e.g.*, Tesla, Inc.), the praises and admonitions of Texas and Delaware, respectively, do not yet reflect a reality of "DExit," or a mass flight of corporates from Delaware to other jurisdictions.

According to a Glass Lewis review of 2025 reincorporation proposals, 28 companies had reincorporation proposals on their ballots, and 18 of those proposed leaving Delaware. Of the 18 companies that proposed leaving Delaware, 13 reincorporated to Nevada while only two proposed reincorporating to Texas (with one such proposal withdrawn before the company's annual meeting). These numbers don't rise to a corporate exodus from Delaware, and in fact, eight companies proposed reincorporating *to* Delaware in 2025.

Further complicating the "DExit" analysis and the proffered improvements that the corporate law of other jurisdictions has to offer, over half of these reincorporation proposals involved companies with significant or controlling shareholders. Included in the Glass Lewis review, a stakeholder commented "states might confuse management friendly policies with business friendly policies," questioning the ultimate recipient of benefits under competing states' corporate laws.

While "DExit" may not yet live up to its name, the attention it is receiving is notable. Actions taken by states like Texas and the support offered by Chairman Atkins indicate perceived cracks in Delaware's dam. However, actions by Delaware corporations, and any additional response by the Delaware legislature may provide insight on whether these cracks as worth patching.

Atkins' Continued Push for Disclosure Reforms: Risk Factors

During his term as Chair of the SEC, Atkins has been active on his campaign to reform Regulation S-K, which sets disclosure requirements for the non-financial aspects of a public company's periodic filings. In his February 17th speech, Atkins reinforced his vision of achieving the "minimum effective dose of regulation" and desire to avoid having rules "drive corporate behavior, rather than reflect the outcome of corporate decisions."

Atkins provided an update on the reform of Item 402, which covers executive compensation disclosures and which following amendments over time Atkins believes has "morphed into a Frankenstein monster beyond recognition." With materiality as the guiding "north star," and rationalization, simplification and modernization as key principles, Atkins previewed three potential reforms to Item 402 suggested by commenters: (1) reducing the number of executives required to be included in Item 402 disclosures, (2) simplifying the pay-versus-performance disclosure and (3) ceasing to treat executive security at a residence or during personal travel (as opposed to at the office or during business travel) as a perk.

In line with his directive to improve the utility of disclosures, Atkins criticized SEC rulemaking that has sought to enforce best practices on governance through "regulation by shaming" and mandated impractical voluminous disclosure.

Atkins also addressed the need for reform in risk factor disclosure. However, unlike in other areas, Atkins believes that the trend towards longer risk factor disclosure is not the result of SEC rulemaking, noting recent amendments have imposed strict page limits (or required a concise summary if limits are not abided by).

Atkins expressed dissatisfaction with the length, complexity, and use of legalese in public companies' risk factor disclosures today. Atkins solicited feedback and offered two potential purposes, asking commentators to consider whether the risk factors should principally: (i) be used as a tool to communicate to investors "what keeps management up at night" or (ii) aid companies to establish liability defenses.

If the former, Atkins suggested that an entity or the SEC develop and maintain a set of generic risks (published separately and omitted from companies' annual reports) that apply broadly across companies and industries. This list could include risk factors related to legislative and regulatory changes, existing and potential geopolitical issues and the chance of a natural disaster—risk factors that apply broadly to most companies and take up pages in annual reports. Instead of preparing their own, a company could refer to this pre-prepared list and supplement it with limited additional risk factors that are specific and material to the company.

If the latter, Atkins proposed that the SEC could adopt a safe harbor from liability. The failure to include generic risk factors in annual reports would not constitute a material omission for some or all federal securities laws' anti-fraud rules. As a result, companies would not feel obligated to include generic risk factors and could include only focused, specific risk factors in filings.

Beyond Item 402 and risk factors, Atkins once again invited comments on Regulation S-K more broadly. As with previous views articulated by Atkins, it remains to be seen whether any amendments to Regulation S-K have the desired

effect of providing investors with a the right level of targeted and concise information without overburdening companies or omitting material disclosure.