

# Clients & Friends Memo

## SEC Proposes Amendments to Modernize Disclosure Requirements

September 18, 2019

The Securities and Exchange Commission has proposed amendments to the business description, legal proceedings and risk factor disclosures required by registered companies in annual and quarterly reports and registration statements. The proposal is meant to modernize disclosure requirements, including by eliminating certain duplicative disclosure requirements and improving the usability of filings for investors. If adopted, the proposed amendments could reduce the amount of repetitive or non-material disclosure in SEC filings, but in some instances, registrants may be required to add disclosure to their SEC filings.

The SEC is currently taking comments on the proposed amendments, which are due on October 22, 2019.

### General Development of Business (Item 101(a))

The proposed amendments to Item 101(a) reflect the SEC's shift towards a "principles-based" approach, where disclosure objectives are set and registrants have more flexibility in determining what disclosure is important for their particular business, and away from the "prescriptive" approach requiring all registrants to disclose the same types of information.

- Qualification of Required Disclosure. Under current Item 101(a), a registrant must make disclosure regarding the general development of the registrant's business, including: bankruptcy and receivership proceedings, merger or consolidation of the registrant or its major subsidiaries, and the acquisition or disposition of a material amount of assets. The proposed rules would require disclosure on these topics only to the extent that the disclosure would be material to understanding the general development of the registrant's business.
- Broadening Discussion Topics. "Material changes to a registrant's previously disclosed business strategy" would be added to the list of disclosure topics. However, the list would also be made non-exclusive, and the registrant would be required to disclose information not otherwise contemplated by the list of disclosure topics if such information would be material to understanding the general development of the registrant's business.

- Elimination of the Five-Year Timeframe. Discussion of the general development of the registrant's business would be made without respect to a specific timeframe. Rather, the registrant would be required to provide information material to an understanding of the development of the business, regardless of the specific timeframe.
- Require Only Updated Disclosure. The proposed rules would require, in filings made after a registrant's initial filing, only an update of the general development of the business with a focus on material developments in the reporting period with a hyperlink to the registrant's most recent filing (e.g., the initial registration statement or more recent filing if one exists) that, together with the update, would contain the full discussion of the general development of the registrant's business.

#### **Narrative Description of Business (Item 101(c))**

The proposed amendments to Item 101(c) follow the "principles-based" approach of the proposed changes to Item 101(a) by eliminating the required disclosure of specific information, and instead requiring the registrant to make disclosures that are more relevant to such registrant's particular business.

- Qualification of Required Disclosure. The current rule regarding the narrative description of a registrant's business lists twelve specific items that must be disclosed to the extent material to an understanding of the registrant's business taken as a whole. The proposed amendments would shorten this list and make the items non-exclusive.
- Human Capital Resources. Under the current rules, the registrant must disclose its current number of employees. The proposed amendments would replace this requirement with a required description of the registrant's human capital resources. This includes "objectives that management focuses on in managing the business," which may change depending on the registrant's industry. The SEC is considering adding non-exclusive examples of such measures to the amendment, including voluntary and involuntary turnover rates, internal rates of hiring or promotion, and number of full-time, part-time, seasonal and temporary workers.
- Government Regulation Compliance. The new rules would broaden the current required discussion of the material impact of environmental regulations on the registrant's business to a required discussion of all material government regulations.

#### **Legal Proceedings (Item 103)**

Changes to the legal proceedings disclosure requirements are meant to modernize the requirements by eliminating duplicative disclosure and using more up-to-date dollar thresholds.

- Cross-references. A registrant would be able to provide required disclosure about legal proceedings by using cross-references or hyperlinks to discussion elsewhere in the filing, such as the registrant's financial statements.

- Higher Threshold for Environmental Proceedings. Current rules require that registrants disclose certain environmental proceedings that could result in sanctions of \$100,000 or greater. The proposed amendments would increase this threshold to \$300,000.

#### **Risk Factors (Item 105)**

Changes to the risk factors disclosure requirements are meant to facilitate an investor's review of those risk factors that are particularly relevant to investing in the registrant.

- Materiality Standard. The new rules would replace the "most significant" risk factors standard with a "material" risk factors standard, which would broaden disclosure to "matters to which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to purchase the security."
- Summary for Lengthy Disclosure. Under the proposed amendments, risk factor disclosures exceeding 15 pages would need to be accompanied by a summary aimed at increasing the utility of the section for an investor.
- Headings and General Risk Factors. The new amendments would require that risk factors be organized under relevant headings, and that any risk factors that could apply generally to other companies or securities offerings would be disclosed at the end of the section under the "General Risk Factors" caption.

\* \* \*

Questions regarding this Client & Friends Memo can be directed to the authors.

William P. Mills	+1 212 504 6000	<a href="mailto:william.mills@cwt.com">william.mills@cwt.com</a>
Erica Hogan	+1 212 504 6000	<a href="mailto:erica.hogan@cwt.com">erica.hogan@cwt.com</a>
Matthew L. Dolloff	+1 212 504 6000	<a href="mailto:matthew.dolloff@cwt.com">matthew.dolloff@cwt.com</a>