

October 13, 2017

# SEC Proposes Rules to Modernize and Simplify Regulation S-K Disclosure Requirements

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## **Proposal Would Streamline MD&A to Provide Flexibility in Discussing Historical Periods and Simplify Exhibit Practices and Related Process for Confidential Treatment Requests**

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### **SUMMARY**

On October 11, 2017, the Securities and Exchange Commission proposed amendments to modernize and simplify disclosure requirements in Regulation S-K and to make parallel amendments to investment company and investment adviser rules and forms. The amendments are intended to improve the readability and navigability of disclosure documents and discourage repetition and disclosure of immaterial information.

The proposed amendments are available on the SEC's website at <https://www.sec.gov/rules/proposed/2017/33-10425.pdf>. Public comments on the proposed amendments will be due within 60 days after publication of the proposed amendments in the Federal Register.

### **BACKGROUND**

In November of last year, the SEC Staff released its "Report on Modernization and Simplification of Regulation S-K," which was mandated in part by Section 72003 of the Fixing America's Surface Transportation Act (the "FAST Act"). The Report (1) provided specific and detailed recommendations on modernizing and simplifying the requirements under Regulation S-K in a manner that reduces the costs and burden on companies while still providing all material information and (2) made recommendations on ways to improve the readability and navigability of disclosure documents and to discourage repetition and

the disclosure of immaterial information. The proposals are based largely on the recommendations in the Report.

The SEC approved the issuance of the proposed amendments to implement the FAST Act mandate at an open meeting held on October 11, 2017, during which two proposals in particular were highlighted by Chair Jay Clayton. He noted that the proposed amendment to the MD&A disclosure requirements would allow for flexibility in discussing historical periods that should discourage repetition of disclosure that is no longer material to investors. Chair Clayton also highlighted that the proposal to allow issuers to omit from exhibits confidential information that is not material and competitively harmful if publicly disclosed would streamline the confidential treatment process and should better safeguard confidential and sensitive information. The SEC has acknowledged that the proposed amendments represent incremental changes to Regulation S-K. They are incremental and largely technical, but the amendments proposed to the exhibit requirements, such as omitting personally identifiable information and exhibits and schedules to material contracts without needing to pursue the confidential treatment request process, are welcome proposals to streamline the disclosure process without impacting the availability of material information for investors.

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### PROPOSED AMENDMENTS

The SEC's proposal addresses multiple items of Regulation S-K and related rules in the 253-page adopting release, which are summarized in the Appendix attached hereto. Of particular note are proposed amendments pertaining to the following areas:

- **Item 303 (Year-to-Year Comparisons in Management Discussion and Analysis).** Item 303(a) requires issuers to discuss their financial condition, changes in financial condition and results of operations. The SEC's proposal would allow issuers to provide a period-to-period comparison only for the two most recent fiscal years covered by the financial statements if (1) the omitted discussion is not material to an understanding of the issuer's financial condition, changes in financial condition and results of operations, and (2) the issuer has filed its prior year Form 10-K containing an MD&A of the earliest of the three years included in the financial statements of the current filing. The SEC is *not* proposing the Staff's recommendation in the FAST Act Report to hyperlink the prior year's annual report for additional period-to-period comparison. Additional proposals to simplify Instruction 1 to Item 303(a) eliminate the reference to five-year selected financial data for trend information and emphasize that an issuer may use any presentation that, in its judgment, would enhance a reader's understanding, including, for example, a narrative discussion in lieu of a year-to-year comparison for some or all of the years in the three-year period.

To maintain a consistent approach to the MD&A disclosure requirements for domestic issuers and foreign private issuers, the SEC is proposing changes to Form 20-F that conform to its proposed amendments to Instruction 1 to Item 303(a) but is not proposing similar changes to Form 40-F (that permits Canadian issuers to use Canadian disclosures to satisfy the SEC's registration and disclosure requirements).

- **Item 601 (Exhibits).** The SEC's proposals on exhibits would:
  - Allow issuers to omit entire schedules and similar attachments to exhibits unless they contain material information and unless that information is not otherwise disclosed in the exhibit or

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the disclosure document, and so long as the issuer provides with each exhibit a list identifying the contents of any omitted schedules and attachments. The issuer is required to provide, upon request of the Staff and on a supplemental basis, a copy of any omitted schedules or attachments to the SEC. This treatment is currently expressly authorized for material plans of acquisition under Item 601(b)(2) of Regulation S-K;

- Permit issuers to omit personally identifiable information (“PII”) without submitting a confidential treatment request and without being required to provide an analysis to redact PII from exhibits; and
- Permit issuers to omit confidential information from material contracts filed as exhibits where such information is both not material and competitively harmful if publicly disclosed, without requiring the submission of a confidential treatment request. An issuer would instead be required to (1) mark the exhibit index to indicate that portions have been omitted; (2) include a prominent statement on the first page of each redacted exhibit that information in the marked sections of the exhibit has been omitted from the filed version; and (3) indicate with brackets where the information has been omitted from the filed version of the exhibit. Under the proposal, the issuer, rather than the Staff, would determine the propriety of the redacted information.

To maintain a consistent approach to the exhibit disclosure requirements, the SEC is proposing conforming changes to Form 20-F, but is not proposing similar changes to Form 40-F.

Other proposed amendments, summarized in the Appendix attached hereto, are incremental changes to Regulation S-K that are intended by the Staff to reduce repetitive and immaterial disclosures (such as the proposed changes to Item 102 describing the registrant’s principal properties) and to make disclosures more accessible through technology (such as additional hyperlink and data tagging requirements).

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### NEXT STEPS

The public comment period will be open for 60 days after publication of the proposed amendments in the Federal Register.

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## APPENDIX

Additional proposed amendments include the following:

- **Item 102 (Description of Property).** Item 102 requires disclosure of the location and general character of the principal plants, mines, and other materially important physical properties of the issuer and its subsidiaries. The SEC is proposing to revise this disclosure requirement to clarify that a description of property is only required to the extent that physical properties are material to the issuer, which would include those properties that are material to the issuer's business, and that disclosure may be provided on a collective basis if appropriate. The SEC is not proposing to revise any of the instructions to Item 102 specific to the mining, real estate and oil and gas industries.
- **Item 401 (Directors, Executive Officers, Promoters and Control Persons).** The SEC's proposal would clarify that the information regarding executive officers described in Item 401 is not required in proxy statements if that information is otherwise provided in the issuer's Form 10-K and change the required caption to "Information about Our Executive Officers" (instead of the current "Executive officers of the registrant").
- **Item 405 (Compliance with Section 16(a) of the Exchange Act).** Item 405 requires issuers to disclose each reporting person who failed to file on a timely basis Section 16 reports. The SEC is proposing to allow issuers to rely on electronically filed reports in determining whether there are any delinquencies required to be reported and eliminate the requirement for Section 16 reporting persons to furnish duplicates of reports filed by them to the issuer. The SEC is also proposing to clarify that while issuers may rely on electronically filed Section 16 reports, they are not required to limit their inquiry to those filings. Finally, the SEC's proposals (1) add an instruction encouraging issuers to exclude the heading "Section 16(a) Beneficial Ownership Reporting Compliance" if there are no delinquencies to report, (2) change that heading to "Delinquent Section 16(a) Reports" to more precisely describe the required disclosure, and (3) eliminate the Form 10-K cover page's check box relating to Item 405 disclosures and the related instruction in Item 10 of Form 10-K.
- **Item 407 (Corporate Governance).** The SEC is proposing to update an outdated reference to AU Section 380 by referring more broadly to the applicable requirements of the Public Company Accounting Oversight Board and the SEC, and to clarify that, like smaller reporting companies, emerging growth companies are not required to provide a compensation committee report.
- **Item 501 (Forepart of Registrant Statement and Prospectus Cover Page).** Item 501 includes disclosure requirements related to the forepart of registration statements and the outside front cover page of prospectuses. The SEC is proposing to:
  - Eliminate the portion of the Instruction to Item 501(b)(1) that discusses when a name change may be required;
  - Explicitly allow a clear statement that the offering price will be determined by a particular method or formula that is more fully explained in the prospectus, so long as a cross-reference (with a prominently highlighted page number) to such disclosure is included;
  - Require disclosure of the principal U.S. market(s) where the issuer's securities are being offered and the corresponding trading symbols and limit disclosure of markets that are not national securities exchanges to those principal United States markets where the issuer, through the engagement of a registered broker-dealer, has actively sought and achieved quotation;
  - Permit issuers to exclude from the prospectus the portion of the "subject to completion" legend relating to state law for offerings that are not prohibited by state blue sky law; and

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- Consolidate Items 501(b)(10) and 501(b)(11) without substantive change, to address all the situations where a “subject to completion” legend is required.
- **Item 503 (Risk Factors).** The SEC proposes to relocate the “Risk Factors” requirements to a new Item 105 in Subpart 100 of Regulation S-K to clarify that risk factors are required by both registration statements on Form 10 and periodic reports. The proposals also eliminate the risk factor examples currently enumerated in Item 503(c).
- **Item 508 (Plan of Distribution).** Item 508 requires disclosure about the plan of distribution for securities in an offering, including information about underwriters. The SEC is proposing to define the term “sub-underwriter” as a dealer that is participating as an underwriter in an offering by committing to purchase securities from a principal underwriter for the securities, but is not itself in privity of contract with the issuer of the securities.
- **Item 512 (Undertakings).** Item 512 provides undertakings that an issuer must include in Part II of its registration statement, depending on the type of offering. The SEC is proposing to eliminate the Item 512(c) undertaking (warrant and rights offerings) as unnecessary and the Item 512(d), Item 512(e), and Item 512(f) undertakings (competitive bids, incorporated annual and quarterly reports, and equity offerings of nonreporting registrants) as obsolete.
- **Item 601 (Exhibits).** The SEC is proposing to:
  - Require issuers to provide the information required by Item 202(a)-(d) and (f) (a brief description of their registered capital stock, debt securities, warrants and rights, other securities and American Depositary Receipts) as exhibits to Form 10-K, while clarifying that Item 202 disclosure is only required for securities that are registered under Section 12 of the Securities Exchange Act of 1934. Currently, Item 202 information is only required in registration statements;
  - Limit the two-year look back period for filing material contracts not made in the ordinary course of business to newly reporting issuers; and
  - Require disclosure of legal entity identifiers (“LEIs”) for the issuer and its significant subsidiaries, if LEIs have been obtained. LEIs are alpha-numeric codes that allow for unique identification of entities engaged in financial transactions.
- **Incorporation by Reference.**
  - **Five-year Limit.** The SEC is proposing to eliminate the Item 10(d) prohibition on incorporating by reference documents that have been on file with the SEC for more than five years. The remaining Item 10(d) provisions (prohibiting indirect incorporation by reference) would be moved to other rules governing incorporation by reference.
  - **Rule 411 under the Securities Act of 1933; Rules 12b-23 and 12b-32 under the Securities Exchange Act of 1934; and Related Rules under the Investment Company Act of 1940 and Investment Advisers Act.** These rules govern incorporation by reference in a variety of contexts, and the SEC is proposing several revisions to modernize the rules and make them more consistent:
    - Eliminate the requirement that copies of information incorporated by reference be filed as exhibits to registration statements or reports, as well as the requirement in Rule 8b-23 under the Investment Company Act that requires investment company issuers to file with a registration statement or report a copy of any registration statement, report, or prospectus from which information is incorporated by reference (where not filed electronically);
    - Require hyperlinks to information that is incorporated by reference if that information is available on EDGAR and expand the requirement to file documents in HTML format to include filings that are subject to the proposed hyperlinking requirements;

### Appendix-2

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- Prohibit incorporation by reference or cross-referencing in financial statements of information from outside the financial statements, except when otherwise specifically permitted by the SEC's rules (for example, cross-references in the financial statements to information outside of the financial statements about segments when that information conforms with generally accepted accounting principles);
  - Restrict the incorporation of financial information required to be given in comparative form for two or more fiscal years or periods, unless the information incorporated by reference includes the entire period for which the comparative data is given and except as otherwise provided in the SEC's rules;
  - Eliminate the requirement that if a certificate of an independent public accountant previously or concurrently filed is incorporated by reference by an investment company (with respect to the filing of a registration statement, application, or report) or an investment adviser (with respect to the filing of an application), a written consent of the accountant must be filed with the filing;
  - Eliminate certain restrictions currently contained in the Investment Company Act and Investment Advisers Act on incorporating by reference exhibits or financial statements made in certain filings; and
  - Replace the current provisions of the Investment Company Act and Investment Advisers Act allowing the SEC to refuse to permit incorporation by reference where, in the SEC's judgment, such incorporation would render a registration statement or report of an investment company or an application filed by an investment adviser incomplete, unclear, or confusing with a general requirement that information cannot be incorporated by reference where such information would render the disclosure incomplete, unclear, or confusing.
- The SEC is also proposing to streamline, clarify, and conform these proposals by eliminating redundant or obsolete rules, relocating existing provisions to other sections, and making conforming revisions to several of its forms to implement the proposed amendments.
  - **Forms.** The proposals amend Form 10, Form 10-K and Form 20-F to allow issuers to exclude item numbers and captions or to create their own captions tailored to their disclosure. The proposal would not affect captions that are expressly required by the forms or Regulation S-K.
  - **Manner of Delivery Recommendations.** The SEC is proposing amendments to require machine-readable Inline XBRL tagging for all information on the cover pages of Form 10-K, Form 10-Q, Form 8-K, Form 20-F, and Form 40-F. If the Inline XBRL proposal is not adopted, the SEC's alternative proposal would be to require operating company filers to tag each cover page data point in an XBRL exhibit to the relevant filing. To implement the cover page tagging requirements, the SEC proposes to require issuers to file with each of the specified forms a "Cover Page Interactive Data File" (to be newly defined as the machine readable computer code that presents the information required by Rule 406 of Regulation S-T in Inline XBRL format). Issuers filing Form 20-F and Form 40-F would be required to tag cover page data only when those forms are used as annual reports and not when used as registration statements.

Additionally, the SEC is proposing to require a ticker symbol for each class of securities registered to be included on the cover pages of Form 10-K, Form 10-Q, Form 8-K, Form 20-F, and Form 40-F and disclosure of the title of each class of securities and each exchange on which they are registered on the cover pages of Form 10-Q and Form 8-K.

Finally, the SEC is proposing amendments to apply hyperlinking and HTML requirements to forms used by and rules applicable to investment companies similar to recently adopted requiring hyperlinks to most exhibits filed pursuant to Item 601, Form F-10, and Form 20-F. For example, these proposals require investment company issuers to file registration statements and reports that include exhibits in HTML format and to include a hyperlink to each exhibit identified in a filing's exhibit index, unless certain exceptions apply.

Appendix-3