



LAW ALERT

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Securities Exchange Commission Modernizes Regulation S-K New Rules Effective on September 22, 2020

The Securities and Exchange Commission has adopted rule amendments to “modernize” SEC reporting company disclosure in periodic reports and registration statements under Regulation S-K. The purpose of the updates is to improve disclosures allowing companies to tailor responses and prioritize material items. The updated Regulation S-K rule items are: Items 101(a) (*General development of business*) and (c) (*Description of business*); Item 103 (*Legal Proceedings*); and Item 105 (*Risk Factors*).

This was the first major update that the SEC has implemented regarding the business disclosure rules in 30 years. In adopting the updated rules, the SEC considered the many changes that have occurred over that period in the capital markets and the domestic and global economy since the adoption of the Regulation S-K disclosure requirements, including changes in the mix of businesses that participate in the public markets, changes in the way businesses operate, changes in technology (in particular technology that facilitates the provision of, and access to, information), and other changes that have occurred simply with the passage of time. Many of the amendments reflect the SEC’s commitment to a principles-based approach to disclosure – one that articulates a disclosure “concept” rather than a hard rule -- that is company specific. The SEC’s disclosure requirements, while prescriptive in some respects, are rooted in materiality and are designed to:

- facilitate an understanding of a company’s business, financial condition and prospects through the lens through which management and the board of directors manage and assess the performance of the company; and
- be flexible enough to continue to allow for fulsome disclosure as businesses evolve in the future.

The SEC believes that modernizing Regulation S-K Items 101, 103, and 105 will result in improved disclosure in more efficient and concise filings, tailored to reflect companies’ particular circumstances, and reduce disclosure costs and burdens. The amended rules also focus on the overall readability of disclosure, opting for a less redundant process and more fluid disclosures, utilizing summarized reports and hyperlinks to cross-referenced documents.

These changes affect many of the regularly timed filings such as annual reports on Form 10-K and quarterly reports on Form 10-Q as well as registration statements.



Highlights of the rule changes:

- Item 101(a) (*General development of business*) is amended in the following ways:
 - It replaces the previously required five-year time-frame with a framework that elicits principles-based disclosure of information material to an understanding of the general development of the company's business.
 - This allows companies to use a reasonable time period that is necessary to disclose material information as they see fit to their circumstances, whether that be a longer or shorter period.
 - It permits a company, in filings made after a company's initial filing, to provide only an update of the general development of the business focused on material developments that have occurred since its most recent full discussion of the development of its business, along with an active hyperlink to earlier filings that has a full discussion of the company's general development of business.
- The SEC also adopted corresponding amendments to Item 101(h) applicable to smaller reporting companies.
- Item 101(c) (*Description of business*) is amended in the following ways:
 - It clarifies and expands the principles-based approach of Item 101(c) with a non-exclusive list of the types of information that companies need to disclose to the extent material to an understanding of the company's business, considering among other things: revenue generating activities, product development, market trends, competitive factors, sources and availability of raw materials and duration and effect of intellectual property. Disclosure will now be required only if the information is material to an understanding of the general development of a company's business taken as a whole.
 - It includes as a disclosure topic, a discussion of the company's human capital resources to the extent that it is material to an understanding of the business, including any human capital measures or objectives that management focuses on in managing the business.
 - It refocuses the regulatory compliance to incorporate all material government regulations (domestic and foreign) as a topic, not just environmental laws.



- Item 103 (*Legal Proceedings*) is amended in the following ways:
 - It states that required information may be provided by hyperlink or cross-reference to legal proceedings disclosure located elsewhere in the document, such as, for example, management's discussion and analysis, risk factors, or a note to the financial statements, to avoid duplication.
 - It increases the existing threshold for disclosure of environmental proceedings to which the government is a party from \$100,000 to \$300,000, but it also allows a company to elect to use a different threshold that is reasonably designed to result in disclosure of material environmental proceedings.
 - This alternative threshold may not exceed the lesser of \$1 million or one percent of the current assets of the company and its subsidiaries on a consolidated basis.
- Item 105 (*Risk Factors*) is amended in the following ways:
 - If the risk factor section exceeds 15 pages, a summary disclosure of risk factors not to exceed two pages is required.
 - It requires disclosure of the most significant factors that make an investment in the company or offering speculative or risky and specifies that the discussion should be concise and organized logically. The principles-based requirement further directs companies to explain how each risk affects the company or the securities being offered, and discourages disclosure of risks that could apply generically to any company.
 - It requires risk factors to be organized under relevant headings with general risk factors applying to an investment in securities to be disclosed at the end of the risk factor section under a separate caption.

The updated rule can be found at <https://www.sec.gov/rules/final/2020/33-10825.pdf>.

The update to Regulation S-K was published in the Federal Register on August 23, 2020 as a proposed final rule, and the SEC published the final rule on August 26, 2020.



When do the updated rules apply?

The updated rules are effective on September 22, 2020 (30 days after being published in the Federal Register). For SEC reporting companies with calendar fiscal-years, the new Item 101(a) (*General development of business*), Item 101(c) (*Description of business*) and Item 105 (*Risk Factors*) (and Item 101(h) for smaller reporting companies) will not apply to its periodic reports until the next Annual Report on Form 10-K. However, these amendments will be in effect before the deadline for Quarterly Reports on Form 10-Q for the period ending September 30, 2020, thus reporting companies need to consider the changes in Item 103 (*Legal Proceedings*) relating to thresholds for environmental proceedings disclosure and the ability to cross reference to legal proceedings elsewhere in the report. A reporting company with a non-calendar fiscal year that has a Form 10-K deadline in the near term following the effectiveness of the amendments will need to be mindful of crafting its disclosure to meet all the new rules.

For more information please contact:

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