

# The Securities and Exchange Commission Simplifies Disclosure Rules

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Capital Markets and Securities

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The Securities and Exchange Commission (the Commission) recently adopted amendments to its disclosure rules to eliminate requirements that it deems “redundant, duplicative, overlapping, outdated, or superseded” based, in part, on other Commission rules and generally accepted accounting principles in the United States (U.S. GAAP).<sup>1</sup> The Commission adopted the amendments “to facilitate the disclosure of information to investors and simplify compliance without significantly altering the total mix of information provided to investors.” At the same time, the amendments are intended to reduce compliance costs for public companies, which the Commission suggests may help encourage capital formation. The amendments primarily affect public companies and are part of the Commission’s implementation of the Fixing America’s Surface Transportation (FAST) Act, which required the Commission to eliminate duplicative, overlapping, outdated, or unnecessary provisions of Regulation S-K. The changes will be effective 30 days after publication in the Federal Register.

The Commission proposed these amendments in July 2016.<sup>2</sup> The final release adopts many of the proposed amendments substantially in the form proposed.

The Commission’s changes can be divided into four categories:

## I. Redundant or Duplicative Requirements

The Commission eliminated from Regulation S-X a number of disclosure requirements that call for substantially similar disclosure as U.S. GAAP, International Financial Reporting Standards (IFRS), or other Commission disclosure requirements. These include provisions relating to, among other items, financial statement consolidation, debt obligations, income tax disclosures, warrants, rights and convertible instruments, identification of related party transactions, material contingencies, and presentation of earnings per share.

## II. Overlapping Requirements

The bulk of the changes fall within this category, which the Commission identified as disclosure requirements that are related to, but not the same as, requirements under U.S. GAAP, IFRS, or other Commission disclosure requirements. For example:

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<sup>1</sup> [Release No. 33-10532](#).

<sup>2</sup> [Release No. 33-10110](#).

- Disclosure about research and development activities required by Items 101(c)(1)(xi) and 101(h)(4)(x) of Regulation S-K and Item 5.C of Form 20-F will no longer be required because substantially similar disclosure is required by U.S. GAAP in the footnotes to the financial statements.
- The Commission deleted requirements in Items 101(d)(1) and 101(d)(2) of Regulation S-K to disclose financial information by geographic area and in Item 101(d)(3) to disclose risks attendant to and dependence on foreign operations on the basis that the risk factors and Management's Discussion and Analysis in periodic reports cover the same information. Additionally, in order to integrate the discussion of a company's ongoing business by geographic area into one location, the Commission eliminated the requirement in Item 101(d)(4) of Regulation S-K to disclose, when interim financial statements are presented, a discussion of the facts that indicate that the three-year financial data for geographic performance may not be indicative of current or future operations. In addition, the Commission amended Item 303(a) of Regulation S-K to require discussion of "geographic areas."
- The Commission deleted Item 101(b) of Regulation S-K and Rule 3-03(e) of Regulation S-X, which require disclosure of financial information by segment, on the basis that U.S. GAAP and Item 303(b) of Regulation S-K require substantially the same information.
- The Commission deleted Instruction 5 to Item 303(b) of Reg. S-K because the seasonality disclosure required by that instruction is covered by U.S. GAAP and other Commission disclosure requirements.
- Because reasonably similar information is required to be disclosed by U.S. GAAP, the Commission eliminated the requirement in Item 201(a)(2)(i) of Regulation S-K to disclose on Form S-1 or Form 10 the amount of common equity subject to outstanding options, warrants, or convertible securities where there is no established United States public trading market for the common equity.
- The Commission deleted the requirement to disclose the frequency and amount of cash dividends in Item 201(c)(1) of Regulation S-K, and amended Rule 3-04 of Regulation S-X to require disclosure of the amount of cash dividends declared in interim periods.
- The Commission eliminated requirements to disclose the historical and pro forma ratios of earnings to fixed charges and earnings to combined fixed charges and preferred stock dividends in registration statements for debt securities and preferred stock, respectively, as well as to file an exhibit showing the computation of such ratios, because the Commission determined that investors can generally calculate such ratios using other financial information required to be disclosed.

In addition, the Commission referred certain disclosure requirements that partially overlap with U.S. GAAP to the Financial Accounting Standards Board (FASB) to determine within 18 months whether U.S. GAAP should be amended. For example, the Commission retained Regulation S-X disclosure requirements related to repurchase and reverse repurchase agreements, but referred the requirements to FASB to determine whether they should be incorporated in U.S. GAAP. In addition, the Commission retained Regulation S-K Item 201(d) disclosure of existing equity compensation plans where equity securities are authorized for issuance, but referred these disclosure requirements to FASB for potential incorporation in U.S. GAAP.

### **III. Outdated Requirements**

The Commission amended requirements that have become outdated as a result of the passage of time or changes in the regulatory, business, or technological environments. For example, due to the availability of information online, the Commission removed requirements to refer to its public reference room and to disclose quarterly high and low trading prices for common stock traded in an established public trading market in annual reports and prospectuses. In addition, the Commission now requires all companies, rather than just accelerated and large accelerated filers, to disclose their website address.

### **IV. Superseded Requirements**

Finally, the Commission amended rules to clean up inconsistencies that have arisen between newer requirements and existing Commission disclosure requirements. For example, the Commission removed the concept of “extraordinary items” from various disclosure requirements because the FASB eliminated extraordinary items from U.S. GAAP in 2015.

### **Legal Proceedings and Loss Contingency Disclosure Remains Unchanged**

In the proposing release, the Commission described the different requirements relating to disclosure of legal proceedings and other loss contingencies under Item 103 of Regulation S-K and Accounting Standards Codification 450, and requested comment on integrating the two disclosure regimes. The Commission received a variety of comments on the subject and decided not to move forward with integrating these disclosure requirements at this time. The Commission also decided not to refer this question to the FASB, pending further consideration of the implications of potential changes.

### **Effect of Amendments**

As a result of the amendments, some information will no longer be disclosed in the forepart of registration statements or periodic reports, and will be located solely within the footnotes to the financial statements. Companies should be mindful that the safe harbor under the Private Securities Litigation Reform Act of 1995 for forward-looking statements will not be available for disclosures that are relocated, pursuant to the amendments, from outside to inside the financial statements. Further, information that is made part of the financial statements will be subject to annual audit and/or interim review, internal control over financial reporting, and XBRL tagging requirements, as applicable.

While none of these amendments individually is significant, as a whole, they represent good progress in the work of the Commission to modernize and synthesize the patchwork of public company disclosure requirements which have built up over the last several decades. In themselves and taken together the amendments will ease, even if only slightly, the disclosure compliance burden for many companies. Further, these amendments are another solid step forward as part of the broader Commission priority to improve disclosure effectiveness more generally.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Capital Markets and Securities practice:

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