A Double-Edged Sword? Examining the Principles-Based Framework of the SEC's Recent Amendments to Regulation S-K Disclosure Requirements

Client Alert | August 31, 2020

On August 26, 2020, as part of its continued effort to update and modernize public company disclosure requirements, the U.S. Securities and Exchange Commission (the "Commission") adopted amendments to Item 101 ("Description of Business"), Item 103 ("Legal Proceedings") and Item 105 ("Risk Factors") of Regulation S-K at an open meeting of the Commission.[1] These amendments, which mark the first time that these disclosure requirements have been substantially updated in over 30 years, were designed to result in improved disclosure, tailored to reflect a registrant's particular circumstances, and reduce disclosure costs and burdens. Many of the amendments reflect the Commission's "long-standing commitment to a principles-based, registrant-specific approach to disclosure," which Commission Chairman Jay Clayton referred to at the open meeting as the "envy of the world."

As discussed in greater detail below, the key changes are:

- Revisions to the rules for the Description of Business to more broadly embrace a principles-based standard identifying a non-exclusive list of topics that may be addressed when material.
- Revisions to the rules for disclosure of Legal Proceedings to confirm the ability to incorporate by reference from other disclosures in the same document and to raise the dollar threshold for disclosing legal proceedings involving environmental protection laws in which the government is a party.
- Revisions to the Risk Factors standards to encourage more concise and company-specific discussions of material factors that make investment in a company or its securities speculative or risky.

In developing the proposed amendments, the Commission stated that it considered input from comment letters received in response to its disclosure modernization efforts, the SEC staff's experience with Regulation S-K arising from the Division of Corporation Finance's disclosure review program, and changes in the regulatory and business landscape since the adoption of Regulation S-K. As a recent example, in response to the COVID-19 pandemic, the Division of Corporation Finance closely monitored registrants' disclosures about how COVID-19 affected their financial condition and results of operations. Division staff observed that the current principles-based disclosure requirements generally elicited detailed discussions of the impact of COVID-19 on registrants' liquidity position, operational constraints, funding sources, supply chain and distribution challenges, the health and safety of workers and customers, and other registrant- and sector-specific matters. Chairman Clayton stated that "[t]he effectiveness of this framework in providing the public with the information necessary to make informed investment decisions has

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proven its merit time and time again as markets have evolved when we have faced unanticipated events."[2] However, this view was not shared by all of the Commissioners, as evidenced by the amendments' adoption by a 3-2 vote, with the two Democratic Commissioners dissenting.

This client alert begins with a general overview of the amendments adopted by the Commission and their practical impact on existing public company disclosure requirements, as well as the arguments raised by the dissent. A table providing a more detailed review of and observations on the amendments is provided at the end of this alert. For a comparison of the Regulation S-K language from before and after the amendments, please refer to the attached Annex A.

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[1] *See* Modernization of Regulation S-K Items 101, 103, and 105, Exchange Act Release No. 33-10825 (August 26, 2020), *available at* https://www.sec.gov/rules/final/2020/33-10825.pdf.

[2] Modernizing the Framework for Business, Legal Proceedings and Risk Factor Disclosures, *available at* https://www.sec.gov/news/public-statement/clayton-regulation-s-k-2020-08-26.

Gibson Dunn lawyers are available to assist in addressing any questions you may have regarding these developments. For additional information, please contact the Gibson Dunn lawyer with whom you usually work, any lawyer in the firm's Securities Regulation and Corporate Governance and Capital Markets practice groups, or the authors:

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