

August 27, 2018

## SEC STREAMLINES DISCLOSURE REQUIREMENTS AS PART OF ITS OVERALL DISCLOSURE EFFECTIVENESS REVIEW

To Our Clients and Friends:

This client alert provides an overview of changes to existing disclosure requirements recently adopted by the Securities and Exchange Commission (the "Commission"). On August 17, 2018, the Commission adopted several dozen amendments (available [here](#)) to existing disclosure requirements to "simplify compliance without significantly altering the total mix of information" (the "Final Rules"). In Release No. 33-10532, the Commission characterized the amended requirements as redundant, duplicative, overlapping, outdated or superseded, in light of subsequent changes to Commission disclosure requirements, U.S. Generally Accepted Accounting Principles ("GAAP"), International Financial Reporting Standards ("IFRS") and technology developments. The Final Rules are largely consistent with the changes outlined in the Commission's July 13, 2016 proposing release, available [here](#) (the "Proposed Rules"). They form part of the Commission's ongoing efforts in connection with the Disclosure Effectiveness Initiative relating to Regulations S-K and S-X and the Commission's mandate under the Fixing America's Surface Transportation ("FAST") Act to eliminate provisions of Regulation S-K that are duplicative, overlapping, outdated, or unnecessary. The Commission adopted the amendments addressed in the Proposed Rules with few exceptions. The Final Rules will become effective 30 days from publication in the Federal Register. In the short term, **issuers and registrants will need to revise their disclosure practices and compliance checklists** in light of the amendments before filing a registration statement or periodic report following effectiveness of the Final Rules.

### I. Summary of Adopted Changes

For certain disclosure requirements that are related to, but not the same as, U.S. GAAP, IFRS, or other Commission disclosure requirements, the Commission: (i) deleted those disclosure requirements that convey reasonably similar information to or are encompassed by the disclosures that result from compliance with overlapping U.S. GAAP, IFRS, or Commission disclosure requirements; and (ii) integrated those disclosure requirements that overlapped, but required information that was incremental to, other Commission disclosure requirements.

#### A. *Deletions of Requirements Covered Otherwise*

The Commission eliminated the following disclosure requirements, as proposed:[1]

- Amount Spent on R&D. The Commission deleted the requirement to disclose amounts spent on research and development activities for all years presented (Item 101(c)(1)(xi) of Regulation S-K) because it is already covered by U.S. GAAP.

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- Financial Information by Segment. The Commission deleted the requirement to disclose financial information (specifically, revenues from external customers, a measure of profit or loss and total assets) about segments for the last three years (Item 101(b) of Regulation S-K),<sup>[2]</sup> because it is already covered by U.S. GAAP.
- Financial Information by Geographic Area. The Commission deleted the requirement to disclose financial information by geographic area (Item 101(d)(2) of Regulation S-K) and risks associated with an issuer's foreign operations and any segment's dependence on foreign operations (Item 101(d)(3) of Regulation S-K), because it is already covered by U.S. GAAP.
- Dividend History. The Commission deleted the requirement to disclose the frequency and amount of cash dividends declared (Item 201(c)(1) of Regulation S-K), because this information is already covered by amended Rule 3-04 of Regulation S-X.
- Ratio of Earnings to Fixed Charges. The Commission deleted the requirement to provide a ratio of earnings to fixed charges (Items 503(d) and 601(b)(12) of Regulation S-K; Instruction 7 to Exhibits of Form 20-F), because U.S. GAAP already provides the disclosure of the components commonly used to calculate these ratios. Issuers no longer need to include this information in an exhibit to their 10-K or in their registration statements.

## ***B. Integrations of Duplicative Requirements***

The Commission integrated the following duplicative disclosure requirements, as proposed:

- Restrictions on Dividends. The Commission consolidated several disclosure requirements related to the restriction of dividends and related items. Where formerly the disclosure requirements were located in parts of both Regulation S-K and Regulation S-X, the Commission consolidated such disclosure requirements for domestic issuers under a single requirement in revised Rule 4-08(e)(3) of Regulation S-X. The disclosure will now only appear in the notes to the financial statements.
- Discussion of Geographic Areas. The Commission integrated the requirement to discuss facts indicating why performance in certain geographic areas may not be indicative of current or future operations by eliminating the requirement from Item 101(d)(4) of Regulation S-K and revising Item 303 of Regulation S-K (which currently requires a discussion regarding elements of income that are not indicative of the issuer's ongoing business), to add an explicit reference to "geographic areas." In addition, the Commission adopted the following clarification as suggested by the commenters: the discussion of income from certain geographic areas under revised Item 303 of Regulation S-K is not required in all circumstances, but only when management believes such discussion would be appropriate to an understanding of the business.

## **C. *Deletions of Outdated Disclosure Requirements***<sup>[3]</sup>

The Commission also eliminated provisions that have become outdated as a result of the passage of time or changes in the regulatory, business, or technological environment (such as stale transition dates and moot income tax instructions), including the following:

- **Available Information.** The Commission deleted the requirement (contained in Item 101(e)(2) and Item 101(h)(5)(iii) of Regulation S-K, Forms S-1, S-3, S-4, S-11, F-1, F-3, and F-4, Item 1118(b) of Regulation AB, and Forms SF-1, SF-3, N-1A, N-2, N-3, N-5, N6, and N-8B-2) to identify the Public Reference Room and disclose its physical address and phone number. The Commission retained the requirement (contained in Item 101(e)(2) of Regulation S-K, and Forms S-1, S-3, S-4, S-11, F-3, F-4, SF-1, SF-3, and N-4) to disclose the Commission's Internet address and a statement that electronic SEC filings are available there and expanded this requirement to Forms 20-F and F-1. The Commission added a requirement to Items 101(e) and 101(h)(5) of Regulation S-K, and Forms S-3, S-4, F-1, F-3, F-4, 20-F, SF-1, and SF-3 that all issuers disclose their Internet addresses (or, in the case of asset-backed issuers, the address of the specified transaction party).
- **Exchange Rate Data.** The Commission deleted the requirement in Item 3.A.3 of Form 20-F that foreign private issuers provide exchange rate data when financial statements are prepared in a currency other than the U.S. dollar insofar as this data is widely available on the internet.
- **Age of Financial Statements.** The Commission added language clarifying the facts and circumstances when foreign private issuers may comply with the aging requirement to include audited financial statements in an initial public offering that are not older than 15 months compared to the 12 months aging requirement. They also deleted the reference to a waiver in Instruction 2 to Item 8.A.4 of Form 20-F.
- **Market Price.** The Commission eliminated the detailed disclosure requirement under Item 201(a)(1) of Regulation S-K related to historical high and low sale prices in light of the fact that the daily market price of most publicly traded securities are easily accessible free of charge on numerous websites that provide more information than is required under Regulation S-K. Such requirements remain in place for issuers with no class of common equity traded in an established trading market; however, for issuers with established trading markets, the Final Rules require the disclosure of the trading symbols used for each class of common equity and the principal foreign public trading market in the case of foreign issuers. In addition, issuers with common equity that is not traded on an exchange are required to indicate, as applicable, that any over-the-counter quotations reflect inter-dealer prices and may not necessarily represent actual transactions. The Final Rules also amended Item 9.A.4 of Form 20-F to be consistent with the adopted amendments to Item 201(a).

## **D. *Amendments to Superseded Disclosure Requirements***<sup>[4]</sup>

The Commission amended disclosure requirements that were inconsistent with recent legislation and more recently updated U.S. GAAP and Commission disclosure requirements. In addition to updating

references to auditing standards in numerous rules and Commission forms and eliminating non-existent or incorrect references and typographical errors, the Final Rules include several substantive changes with both generally applicable and industry-specific effects in light of changes to U.S. GAAP requirements, including the following:

- Sale of REIT Property. The Commission eliminated the requirement that REITs present separately all gains and losses on the sale of properties outside of continuing operations (Rule 3-15(a)(1) of Regulation S-X), insofar as U.S. GAAP rules require only the presentation of gains and losses on the disposal of "discontinued operations."
- Insurance Companies. The Final Rules include changes applicable to Insurance Company issuers. The Commission removed elements of disclosure requirements regarding reinsurance recoverable on paid losses and the reporting of separate account assets (Rules 7-03(a)(6) and 7-03(a)(11) of Regulation S-X) that conflict with U.S. GAAP.
- Consolidated and Combined Financial Statements. The Final Rules include several changes to Regulation S-X related to the presentation of consolidated and combined financial statements in order to reflect changes to U.S. GAAP. Specifically, the Commission corrected for numerous inconsistencies with respect to Differences in Fiscal Periods (Rule 3A-02 of Regulation S-X), the Bank Holding Act of 1956 (Rule 3A-02 of Regulation S-X), Intercompany Transactions (Rules 3A-04 and 4-08 of Regulation S-X) and Dividends Per Share in Interim Financial Statements (Rules 3-04, 8-03, and 10-01 of Regulation S-X).

## ***E. Deletion of Redundant or Duplicative Requirements***<sup>[5]</sup>

The Commission deleted all duplicative requirements identified in the Proposed Rules, primarily under Regulation S-X, that require substantially similar disclosure as required under U.S. GAAP, IFRS, or other Commission requirements (with the exception of the requirements in Rule 3-20 of Regulation S-X related to the foreign currency disclosure in the financial statements of foreign private issuers). These minor amendments deleted duplicative language covering a wide variety of disclosure topics, including the following:

- Consolidation. The Commission deleted Rule 4-08(a) of Regulation S-X requiring compliance with Article 3A (duplicative of Article 3A), Rule 3A-01 of Regulation S-X stating the subject matter of Article 3A (duplicative of Article 3A), language in Rule 3A-02(b)(1) of Regulation S-X permitting consolidation of an entity's financial statements for its fiscal period if the period does not differ from that of the issuer by more than 93 days (duplicative of ASC 810-10-45-12), language in Rule 3A-02(d) of Regulation S-X requiring consideration of the propriety of consolidation under certain restrictions (duplicative of ASC 810-10-15-10), language in Rule 3A-02 and 3A-03(a) of Regulation S-X requiring disclosure of the accounting policies followed in consolidation or combination (duplicative of ASC 235-10-50-1 and ASC 810-10-50), and language in Rule 3A-04 of Regulation S-X requiring the elimination of intercompany transactions (duplicative of ASC 323-10-35-5a and ASC 810-10-45).

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- Income Tax Disclosure. The Commission deleted language in Rule 4-08(f) of Regulation S-X requiring income tax rate reconciliation (duplicative of ASC 740-10-50-12) and language in Rule 4-08(h)(2) of Regulation S-X permitting income tax rate reconciliation to be presented in either percentages or dollars (duplicative of ASC 740-10-50-12).
- Earnings Per Share. The Commission deleted language in Rule 10-01(b)(2) of Regulation S-X requiring presentation of earnings per share on interim income statement (duplicative of ASC 270-10-50-1b) and Item 601(b)(11) of Regulation S-K and Instruction 6 to "Instructions as to Exhibits" of Form 20-F requiring disclosure of the computation of earnings per share in annual filings (duplicative of ASC 260-10-50-1a, Rule 10-01(b)(2) of Regulation S-X, and IAS 33, paragraph 70).
- Interim Financial Statements. The Commission deleted Rule 10-01(b)(5) of Regulation S-X requiring disclosure of the effect of discontinued operations on interim revenues, net income, and earnings per share for all periods presented (duplicative of ASC 205-20-50-5B, ASC 205-20-50-5C, ASC 260-10-45-3, and ASC 270-10-50-7) and language in Rule 10-01(b)(3) of Regulation SX requiring that common control transactions be reflected in current and prior comparative periods' interim financial statements (duplicative of ASC 805-50-45-1 to 5).
- Bank Holding Companies. The Commission deleted Rule 9-03.6(a) of Regulation S-X requiring disclosure of the carrying and market values of securities of the U.S. Treasury and other U.S. Government agencies and corporations, securities of states of the U.S. and political subdivisions, and other securities (duplicative of ASC 320-10-50-1B, ASC 320-10-50-2, ASC 320-10-50-5, and ASC 942-320-50-2), Rule 9-03.7(d) of Regulation S-X requiring disclosure of changes in the allowance for loan losses (duplicative of ASC 310-10-50-11B(c)), and language in Rule 9-04.13(h) of Regulation S-X requiring disclosure of the method followed in determining the cost of investment securities sold (duplicative of ASC 235-10-50-1 and ASC 320-10-50-9b).

## II. Summary of Proposed Rules Not Adopted

### A. *Retained Requirements*

The Commission originally proposed to delete the following overlapping disclosure requirements, but instead chose to retain the requirements without amendment:

- Pro-Forma Dispositions. The Commission retained the requirement under Rule 8-03(b)(4) of Regulation S-X to present pro forma financial information regarding business dispositions. This decision was in response to commenter concerns that the disclosure would not be sufficiently substituted by Regulation S-K, because Item 9.01 of Form 8-K only references significant acquisitions rather than dispositions. The Commission determined that the issue warranted additional analysis and consideration and opted not to amend the requirement.
- Seasonality. The requirement to discuss seasonality under Item 101(c)(1)(v) of Regulation S-K was retained without amendment. This decision was in response to concerns about the potential

loss of information in the fourth quarter about the extent to which an issuer's business is seasonal because U.S. GAAP may not elicit this disclosure.

- Legal Proceedings. The Commission declined to adopt amendments to the legal proceedings disclosure required under Item 103 of Regulation S-K or to refer the disclosure requirements under Item 103 to the FASB for potential incorporation into U.S. GAAP. The Commission cited several differences between the Regulation S-K requirement and its parallel requirement under U.S. GAAP, and emphasized that integration could have broad implications such as expanding costly audit reviews and increasing the disclosure of immaterial items.
- Mutual Life Insurance Companies. The Commission did not adopt the proposed change to Rule 7-02(b) of Regulation S-X, which would have eliminated the ability of mutual life insurance companies to prepare financial statements in accordance with statutory accounting requirements.

## ***B. Potential Changes Referred to FASB For Prompt Review***

The Commission originally proposed to delete the following overlapping disclosure requirements, but instead opted to retain these requirements and refer them to the Financial Accounting Standards Board ("FASB"), with a request that FASB complete its review within 18 months of the publication of the Final Rules in the Federal Register:

- Repurchase and Reverse Repurchase Agreements. The Commission retained the Regulation S-X disclosure requirements related to repurchase and reverse repurchase agreements (such as the separate presentation of repurchase liabilities on the balance sheet). The Commission emphasized that several commenters had expressed concern that deletion of this requirement would eliminate disclosures that are material and not otherwise available to investors in the repo market.
- Equity Compensation Plans. The Commission also retained the requirement under Item 201(d) of Regulation S-K to discuss securities authorized under equity compensation plans in an information table, noting commenter concerns that U.S. GAAP does not require certain information, such as the number of securities available for issuance under an equity compensation plan, which may be material to investors.

## ***C. Retained Requirements Referred to FASB for Potential Review***

For disclosure requirements that overlapped with, but required information incremental to, U.S. GAAP, the Commission elected to solicit further comment before determining whether to retain, modify, eliminate, or refer them to FASB for potential incorporation into U.S. GAAP.<sup>[6]</sup> In the Final Rules, the Commission generally retained and referred such requirements to FASB to be considered in its normal standard-setting process. For example:

- Major Customers. The Commission retained the requirement to discuss major customers under Item 101(c)(1)(vii) of Regulation S-K despite it being substantially similar to U.S. GAAP requirements, because Regulation S-K (unlike U.S. GAAP) contains an incremental requirement

to disclose the name of a major customer in certain instances. The Commission referred this particular requirement to FASB because it continues to believe the identity of major customers represents material information to investors and allows investors to better assess the risks associated with a particular customer.

- Revenue from Products and Services. While Regulation S-K and U.S. GAAP both require the disclosure of the amount of revenue from products and services, Item 101(c)(1)(i) of Regulation S-K only requires this information if a certain threshold is met, while U.S. GAAP includes a "practicability" exception. Accordingly, the Commission retained and referred the Regulation S-K requirement to FASB for potential incorporation into U.S. GAAP.

## Conclusion

The amendments contained in the Final Rules are highly technical and are explicitly intended to avoid any substantive changes to the "total mix of information provided to investors." Nonetheless, these changes should reduce the cost and time of issuer compliance both by eliminating specific outdated and superfluous disclosure requirements and by reducing the overall number of rules to consider. In the short term, issuers and registrants will need to revise their disclosure practices and compliance checklists in light of the amendments before filing a registration statement or periodic report following effectiveness of the Final Rules.

Furthermore, issuers should expect additional changes in the future as part of the Commission's ongoing efforts to clean up and modernize disclosure requirements in connection with its Disclosure Effectiveness Initiative.

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[1] For a complete discussion on final adoptions for overlapping disclosure requirements proposed to be deleted, see page 37 of the Final Rules.

[2] Additionally, the Commission eliminated Rule 3-03(e) of Regulation S-X as suggested by a commenter (which was not in the Proposed Rules), because it is likewise redundant with U.S. GAAP (see page 71 of the Final Rules).

[3] A complete discussion of adopted amendments for outdated disclosure requirements begins on page 100 of the Final Rules.

[4] A complete discussion of adopted amendments for superseded disclosure requirements begins on page 108 of the Final Rules.

[5] A complete discussion of adopted amendments for redundant or duplicative disclosure requirements begins on page 28 of the Final Rules.

[6] For a complete discussion on overlapping disclosure requirements where the Commission solicited comments see page 83 of the Final Rules.



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

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