

A DOUBLE-EDGED SWORD? EXAMINING THE PRINCIPLES-BASED FRAMEWORK OF THE SEC'S RECENT AMENDMENTS TO REGULATION S-K DISCLOSURE REQUIREMENTS

To Our Clients and Friends:

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

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>.

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 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.

I. The Disclosure Amendments: A Principles-Based Approach

A. Description of Business (Item 101 of Regulation S-K)

The Description of Business disclosure generally appears only in the Annual Report on Form 10-K and in certain registration statements, including Form S-1 and Form 10. Currently, Item 101(a) requires a registrant to discuss the general development of its business during the last five years and states that a longer period may be addressed if material to an understanding of the business.³ Item 101(c) further requires a registrant to address 12 specific topics if those topics are material to the registrant's business.⁴ For example, if such disclosure would be material to its business, a registrant is required to disclose the practices of the registrant and its industry relating to working capital items.

The amendments to Item 101(a), which concerns the general development of the registrant's business, apply a more principles-based framework, eliminating the reference to a five-year timeframe and requiring disclosure of events that would be material to an understanding of the general development of the business. The amendments also allow registrants to provide only updates on material developments in the business or to the business strategy that have occurred since its most recent full discussion of the development of its business in a prior filing, with the prior disclosure incorporated by reference.

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>.

³ See 17 C.F.R. § 229.101(a).

⁴ See 17 C.F.R. § 229.101(c).

Item 101(c), which concerns a narrative description of the registrant’s business, is similarly amended to use a principles-based approach and provide more flexibility. Instead of a set of 12 topics that “shall” be discussed if material, the amendments retain the general subject matter for disclosure (“the business done or intended to be done by the registrant,” with a focus on each reportable segment), but set forth a non-exclusive list of seven topics that the disclosure “may include, but should not be limited to.” Commissioner Elad L. Roisman stated his belief that the new approach would allow registrants to more clearly present information that they consider material in running their businesses.⁵

The non-exclusive list of disclosure topics includes some of the current 12 topics, but in many cases removes prescriptive or qualifying standards. For example, the amended language calls for a discussion of material government regulations, whereas the current rule specifically addresses only environmental regulations. We note that many registrants already include a discussion of material applicable government regulations despite the fact that the current rules do not explicitly require such disclosure. The amendments also add new topics, such as trends in market demand.

Of particular note is that the amended list of disclosure topics includes “[a] description of the registrant’s human capital resources.” This item received particular attention at the Commission meeting at which the rules were adopted and in the Commissioners’ public statements. Chairman Clayton specifically lauded the inclusion of human capital as a disclosure topic, stating that “[f]rom a modernization standpoint, today, human capital accounts for and drives long-term business value in many companies much more so than it did 30 years ago.”⁶ The amendments do not include any specific human capital reporting framework or define “human capital.” Instead, the amendments use a principles-based approach regarding the human capital-related resources, measures and objectives that a registrant focuses on in managing its business. The amendments stress the need for each registrant to consider how to make its disclosure specific to its industry and workforce approach and relevant to its unique facts and circumstances. Chairman Clayton stated that he expects “to see meaningful qualitative and quantitative disclosure, including, as appropriate, disclosure of metrics that companies actually use in managing their affairs” and that “[a]s is the case with non-GAAP financial measures, [he] would also expect companies to maintain metric definitions constant from period to period or to disclose prominently any changes to the metrics used or the definitions of those metrics.”⁷

⁵ See Opening Remarks at the Open Commission Meeting to Adopt Amendments to Items 101, 103, and 105 of Regulation S-K, available at <https://www.sec.gov/news/public-statement/roisman-reg-sk-2020-08-26>.

⁶ See Footnote 2, *supra*.

⁷ *Id.*

B. Legal Proceedings (Item 103 of Regulation S-K)

Item 103 requires a registrant to disclose any material pending legal proceedings, other than ordinary routine litigation incidental to the registrant's business, to which the registrant or any of its subsidiaries is a party or of which any of their property is the subject.⁸ This requirement remains unchanged by the amendments. However, in an effort to eliminate duplicative disclosure,⁹ the amendments expressly confirm that a registrant may provide the information required by Item 103 by hyperlink or cross-reference to a separate disclosure located elsewhere in the document.¹⁰

Currently, the instructions to Item 103 provide that governmental environmental proceedings that involve potential monetary sanctions of \$100,000 or more must be disclosed. This quantitative threshold has resulted in disclosure of environmental proceedings that are immaterial to registrants. The amendments raise this threshold to require disclosure of environmental proceedings involving potential monetary sanctions of \$300,000 or more, but allow a registrant to establish a different disclosure threshold as high as \$1 million (or, if lower, one percent of the current assets of the registrant), provided that the registrant discloses that threshold in each of its annual and quarterly reports.

C. Risk Factors (Item 105 of Regulation S-K)

Currently, Item 105 requires disclosure of the most significant factors that make investing in the registrant speculative or risky.¹¹ Over time, the length of the Risk Factors section has generally increased, driven by developments in private securities litigation and the emergence of new areas and types of risk. Against this backdrop, the Commission stated its concern that, in many cases, generic and boilerplate risks that could apply to any registrant have contributed to the increased length of risk factors, limiting the helpfulness of the disclosure to investors.¹²

The amendments to Item 105 attempt to counter the current trend toward ever-expanding risk factor disclosures in three ways.

First, the amendments require all risk factors to be grouped and organized under relevant headings. Generic risk factors that could apply to any registrant or any offering are required to be disclosed at the end of the Risk Factors section under the heading "General Risk Factors."

⁸ See 17 C.F.R. § 229.103.

⁹ For more information about the SEC's efforts to streamline duplicative disclosures, please refer to our client alert available at this [link](#).

¹⁰ Exchange Act Rule 12b-23, Instruction G(1) of Form 10-K and Instruction D.2. to Form 10-Q already allowed for this type of cross-reference and incorporation by reference.

¹¹ See 17 C.F.R. § 229.105.

¹² See Footnote 1, *supra* at 65-66.

Second, the amendments change the standard for risk factors by requiring disclosure of “material” factors, instead of “the most significant” factors that make an investment speculative or risky. Other wording changes emphasize that risk factors should “concisely” explain how each risk affects the registrant or its securities.

Finally, if a registrant’s Risk Factors section exceeds 15 pages, the amendments require inclusion of a summary risk factor section that is no more than two pages long. The summary must comprise “concise, bulleted or numbered statements summarizing the principal factors that make an investment in the registrant or offering speculative or risky.” A summary risk factor section such as this is already generally included in the prospectus summary for registration statements.

Interestingly, Commissioner Hester M. Peirce said she views the risk factors amendment as a “bit of an experiment,” asking whether the “penalty of having to prepare a summary [will] be sufficient to overcome the fear of litigation that pushes companies to disclose many pages of risks.”¹³

D. Effective Date and Next Steps

The final rules as amended will be effective 30 days after publication in the [Federal Register](#). As of the date of this alert, the final rules had not been published.

As a result, the amendments may be in effect at the time registrants file their Form 10-Q for the third quarter of 2020. Accordingly, a registrant that voluntarily repeats its risk factors in each Form 10-Q may need to reorganize, caption and revise its risk factors prior to filing the next Form 10-Q, or determine whether to only provide any material changes from risk factors that were previously disclosed in the registrant's Form 10-K or prior Form 10-Qs.¹⁴

The amendments will have a greater impact on the content of the Form 10-K for 2020. Registrants should expect to devote additional time to drafting and disclosure committee review of their next Form 10-K. The amendments will also impact the content of securities offering documents, including registration statements for IPOs and spin-offs and presumably private placement offering memorandum. The table presented in Part IV of this alert can serve as a tool in implementing the amendments.

¹³ Statement at Open Meeting on Modernization of Regulation S-K 101, 103, and 105, *available at* <https://www.sec.gov/news/public-statement/peirce-reg-s-k-2020-08-26>.

¹⁴ Item 1A to Form 10-Q only requires disclosure of material changes from those disclosed in a registrant’s Form 10-K, and Exchange Act Rule 12b-23 and Instruction D.2. to Form 10-Q allow risk factors that were disclosed in prior 10-Qs to be incorporated by reference.

II. The Dissent: Calls for a Different Approach

In their respective public statements,¹⁵ Commissioner Allison Herren Lee and Commissioner Caroline Crenshaw pushed back on the enhanced, principles-based approach reflected in the new rules, voicing their dissent at the lack of specific disclosure requirements concerning Environmental, Social and Governance (ESG) matters. Specifically, the dissents focused on the absence of prescriptive rules requiring disclosures and metrics addressing diversity, climate change risk and human capital.

In response, Commissioner Peirce stated in a closing comment at the open meeting of the Commission that the dissent's approach was more prescriptive-based than principles-based and the changes the dissenters' advocated would require a more complete review of the entire disclosure framework. In an exchange between the two, Commissioner Lee did not completely decry the use of the principles-based approach, stating instead that a different approach was needed.

A. Human Capital

Despite the emphatic praise given to the inclusion of human capital as a disclosure topic under Item 101 by some members of the Commission, Commissioners Crenshaw and Lee expressed their view that the amendments do not contain adequate disclosure requirements regarding human capital. Commissioner Crenshaw suggested that, by requiring standardized disclosures around how a registrant manages and invests in its people, investors would be better able to assess how a registrant would perform in a crisis such as the COVID-19 pandemic. Commissioner Lee stated, "I would have supported today's final rule if it had included even minimal expansion on the topic of human capital to include simple, commonly kept metrics such as part time vs. full time workers, workforce expenses, turnover, and diversity."

B. Climate Risk

Both dissenters also focused on the absence of disclosure requirements relating to climate change, including the risks created thereby. Commissioner Lee expressed the concern that the Commission "failed to include, or even discuss whether to include, the crucial topic of climate risk."¹⁶ While acknowledging that the Commission has issued guidance related to the discussion of climate risks, both Commissioners cited investor comments as evidence that the current rules and guidance under the principles-based regime are inadequate.

¹⁵ See Regulation S-K and ESG Disclosures: an Unsustainable Silence, available at <https://www.sec.gov/news/public-statement/lee-regulation-s-k-2020-08-26>; see Statement on the "Modernization" of Regulation S-K Items 101, 103, and 105, available at <https://www.sec.gov/news/public-statement/crenshaw-statement-modernization-regulation-s-k>.

¹⁶ Regulation S-K and ESG Disclosures: an Unsustainable Silence, available at <https://www.sec.gov/news/public-statement/lee-regulation-s-k-2020-08-26>.

C. Diversity

An additional point of focus for the two dissenters was the absence in the amendments of requirements for disclosure regarding diversity. In support of the contention that diversity may be material to an investment decision, Commissioner Lee noted that a recent study found that companies in the top quartile for ethnic diversity on executive teams outperformed those in the bottom quartile by 36 percent in profitability.

III. Gibson Dunn Perspectives and Recommendations

The amendments represent an important step towards modernizing the disclosure framework in the United States, removing detailed and prescriptive standards that are either duplicative of other disclosure requirements or, for many registrants, simply not material. While the principles-based approach could lead to a lack of comparability for investors among registrants' reports, it also could fail to achieve the goal of providing more informative disclosures if the absence of technical guidance or requirements results in excessive disclosures. How the new framework is applied by registrants will evolve and develop over time and be shaped by guidance from the Commission and its staff, the demands of the capital markets, and developments in securities litigation.

The increased regulatory reliance on principles-based standards could prove to be a double-edged sword. On the one hand, registrants will have greater license to adapt their disclosures to reflect their particular business model and operations, which is increasingly important in an innovative and dynamic economy where many aspects of companies' operations defy simple classifications. Moreover, permitting registrants to omit disclosure of information when it is not material may reduce registrant compliance costs. While some commenters are concerned that the move away from prescriptive disclosure standards will allow registrants to avoid addressing some topics, advocates for principles-based standards view that concern as ignoring the pressures of the capital markets and investor demands, which are sophisticated and already lead registrants to address topics not specifically identified in the Commission's existing rules. As noted by the Commission, this has been borne out by many registrants' disclosures during the COVID-19 pandemic.

On the other hand, the Commission noted that a principles-based disclosure framework relying on registrants' determinations of the importance of information to investors could result in increased information asymmetries between registrants and investors if registrants misjudge what information is material. While it said that such asymmetries may increase the cost of capital, reduce capital formation, and hamper efficient allocation of capital across companies, the Commission viewed the risk as being reduced by mitigants such as corporate internal controls and the risk of antifraud litigation.

A principles-based system may also make it more difficult for a registrant to demonstrate its compliance with the Commission's rules, presenting the risk of questioning and second-guessing

by Commission staff in hindsight, either through the comment or enforcement processes, and by class action plaintiffs. While materiality has been and remains the overriding standard, the prescriptive list of topics contained in Item 101 prior to these amendments has served as a useful touchstone for registrants.

As registrants consider changes to their disclosure, it will be important for registrants to assess and potentially adjust their disclosure controls and procedures, including examining their processes for assessing materiality and documenting determinations regarding disclosures and ensuring that disclosure committees and others involved in their disclosure processes are mindful of the need to focus on the principles-based standards.

This principles-based set of requirements also could lead, over time, to inconsistent discretion on the part of the Commission staff when determining whether registrants have complied with the requirements of Regulation S-K. This could increase the cost and length of a review process (whether routine or for a capital markets transaction, which have become increasingly streamlined in recent years), which is inconsistent with the Commission's stated policy position of lowering the burden of being a public company and promoting capital raising.

Notwithstanding the absence of prescriptive standards, we expect human capital disclosure to evolve, as it has already in the midst of the COVID-19 pandemic, and the demand from investors for disclosure about climate risk to continue. In an election year, it is worth noting that both dissenting Commissioners are Democrats. Thus, depending on the outcome of the elections in November, future developments in disclosure requirements could reflect the views expressed in their dissents.

In the meantime, one of the biggest open questions will be with respect to disclosure regarding a registrant's "human capital resources, including ... any human capital measures or objectives that the registrant focuses on in managing the business." This question must be evaluated in a manner tailored to the specific registrant and its workforce. To protect against excessive and unnecessary detail, a company should bear in mind that the federal securities laws and the principles-based framework of the amendments continue to turn on the concept of materiality. In a sense, this exercise is similar to conducting a SAB 99 analysis of human capital factors to identify those that are truly material using the established legal standard (*i.e.*, that there is a substantial likelihood that a reasonable investor would view this as altering the total mix of information).

As a practical matter, management should begin by (1) reviewing their existing internal and external statements regarding key human capital resources, measures and objectives, (2) reviewing their past engagement with and input from shareholders on this topic, and (3) reviewing the list of disclosure topics suggested in the adopting release.¹⁷ Management should be mindful that the

¹⁷ The amended Item 101 provides the following examples, "depending on the nature of the registrant's business and workforce: measures or objectives that address the development, attraction and retention of personnel."

disclosure should be focused on the resources, measures, and/or objectives that are used in managing the company *and* are material to an understanding of the business as a whole. Only certain information will rise to this level. Not every aspect of human capital management that the board or senior management monitors, or that the company may already voluntarily report in a sustainability or human capital report, necessarily rises to the level of being material enough to discuss in the Description of Business section of the Form 10-K. Moreover, the fact that certain investors may be focused on particular aspects of human capital does not mean that the information is material to investors seeking to understand the registrant's business as a whole.

As recognized by the Commission, there are a wide range of issues and degree of focus on human capital management at different companies and in different industries. Thus, we should expect the disclosures to vary widely among industries and companies, and to evolve over time.

The adopting release asked commenters whether the SEC should include other examples in the amendments and specifically mentioned the following possibilities:

- number and types of employees, including the number of full-time, part-time, seasonal and temporary workers;
- measures with respect to the stability of the workforce, such as voluntary and involuntary turnover rates; measures regarding average hours of training per employee per year;
- information regarding human capital trends, such as competitive conditions and internal rates of hiring and promotion;
- measures regarding worker productivity; and
- the progress that management has made with respect to any objectives it has set regarding its human capital resources.

The adopting release also noted that the following human capital topics were suggested by commenters (many of whom are recurring shareholder proposal proponents) in response to the Staff's earlier concept release:

- worker recruitment, employment practices, and hiring practices;
- employee benefits and grievance mechanisms;
- employee engagement' or investment in employee training;
- workplace health and safety;
- strategies and goals related to human capital management and legal or regulatory proceedings related to employee management;
- whether employees are covered by collective bargaining agreements; and
- employee compensation or incentive structures.

IV. Detailed Description of the Amendments and Sample Recommendations

Regulation S-K Item	Existing Item Requirements	New Item Requirements
<u>Item 101(a)(1)</u>	<ul style="list-style-type: none"> • Prescribed a five-year timeframe for disclosure of general developments of a registrant’s business, but with exceptions. • Disclosure should include the year in which a registrant was formed. 	<ul style="list-style-type: none"> • The five-year disclosure timeframe has been eliminated. • Disclosure may include, but is not limited to, the topics specifically addressed in the provision, subject to a materiality standard. • If material, disclosure should include any material changes to a previously disclosed business strategy. • Disclosures of the year and form of organization and any material changes to the mode of conducting business are no longer specifically required.
	<p><u>Gibson Dunn Comment:</u> Companies should be sure their disclosure covers information that is material to an understanding of the general development of their business, including any changes in strategy.</p>	
<u>Item 101(a)(2)</u>	<ul style="list-style-type: none"> • No previous equivalent. 	<ul style="list-style-type: none"> • A registrant can provide an update to the general development of its business by disclosing all of the material developments that have occurred since the most recent registration statement or report that includes a “full discussion” of the general development of its business and then hyperlinking or incorporating by reference the prior “full discussion.”
	<p><u>Gibson Dunn Comment:</u></p> <ul style="list-style-type: none"> • This new provision may be of utility primarily for companies that do not frequently update their business development disclosures. For many companies that have relatively short disclosures or that frequently update their disclosures, the provision may not be too useful. • While an update can incorporate by reference a single prior disclosure, interpretive guidance may be needed on how this provision interacts with the “no double incorporation by reference” provisions of Securities Act Rule 411(e) and Exchange Act Rule 12b-23(e). 	
<u>Item 101(c)</u>	<ul style="list-style-type: none"> • While focusing on disclosure regarding reportable segments, the provision sets forth a list of 12 disclosure topics that shall be addressed if material to the registrant’s business taken as a whole. 	<ul style="list-style-type: none"> • The amended rules continue to focus on disclosure of reportable segments, but calls generally for disclosure of information material to an understanding of the registrant’s business as a whole, including but not limited to seven topics listed in the provision.

<p>Segment-Level Disclosure Requirements</p>	<ul style="list-style-type: none"> • Disclosure topics from the current rule that have been significantly revised include the following: 	<ul style="list-style-type: none"> • As revised, the disclosure topics address the following:
	<ul style="list-style-type: none"> ○ The principal products produced and services rendered by the segment, and the principal markets for, and methods of distribution of, the segment’s principal products and services. ○ The amount or percentage of total revenue contributed by any class of similar products or services which accounted for 10% or 15% or more of consolidated revenue in any of the last three years. ○ The dependence of the segment upon a single customer, or a few customers, and in certain cases the name of any ≥10% customers. 	<ul style="list-style-type: none"> ○ Revenue-generating activities, products and/or services, and any dependence on revenue-generating activities, key products, services, product families or customers, including governmental customers.
	<ul style="list-style-type: none"> ○ The status of a product or segment if there has been a public announcement of, or if the registrant otherwise has made public information about, a new product or segment that would require the investment of a material amount of the assets of the registrant or that otherwise is material. ○ Competitive conditions in the business including the markets in which the registrant competes, the number of competitors, the registrant’s competitive position, and the principal methods of competition. 	<ul style="list-style-type: none"> ○ The status of development efforts for new or enhanced products, trends in market demand and competitive conditions.
<p>Segment-Level Disclosure Requirements</p>	<ul style="list-style-type: none"> • Disclosure topics from the current rule that have been retained without significant revisions include the following: 	<ul style="list-style-type: none"> • The disclosure topics now address the following:
	<ul style="list-style-type: none"> ○ The sources and availability of raw materials. ○ The importance to the segment and the duration and effect of all patents, trademarks, licenses, franchises and concessions held. 	<ul style="list-style-type: none"> ○ All resources material to a registrant’s business (including, for example, the sources and availability of raw materials and the importance to the segment and the duration and effect of all patents, trademarks, licenses, franchises and concessions held).
	<ul style="list-style-type: none"> ○ A description of any material portion of the business that may be subject to renegotiation of profits or termination 	<ul style="list-style-type: none"> ○ Same

	of contracts or subcontracts at the election of the Government	
	<ul style="list-style-type: none"> ○ The extent to which the business is or may be seasonal 	<ul style="list-style-type: none"> ○ Same
Segment-Level Disclosure Requirements	<ul style="list-style-type: none"> · Disclosure topics from the current rule that have been eliminated include the following: 	
	<ul style="list-style-type: none"> ○ The practices of the registrant and the industry relating to working capital items such as inventory requirements, rights to return merchandise, and providing extended payment terms. ○ The dollar amount of backlog orders currently and in the preceding year, and the portion not reasonably expected to be filled in the current year. 	
	<p><u>Gibson Dunn Comment:</u> Although the foregoing topics have been dropped as topics to be specifically addressed, companies should continue to evaluate whether these topics are material to an understanding of the registrant’s business as a whole, and if so to continue addressing them.</p>	
Company-Level Disclosure Requirements	<ul style="list-style-type: none"> · Disclosure topics from the current rule that have been significantly revised include the following: 	<ul style="list-style-type: none"> · As revised, the disclosure topics address the following:
	<ul style="list-style-type: none"> ○ The material effects that compliance with laws that protect the environment may have on capital expenditures, earnings and competitive position, including any material estimated future capital expenditures for environmental control facilities. ○ The number of persons employed. 	<ul style="list-style-type: none"> ○ The material effects that compliance with all government regulations (not just environmental regulations), may have on capital expenditures, earnings, and competitive position, including the estimates capital expenditures for environmental control facilities. ○ Human capital resources, the number of persons employed by the registrant, and any human capital measures or objectives that the registrant focuses on in managing the business (such as, depending on the nature of the registrant’s business and workforce, measures or objectives that address the development, attraction and retention of personnel).

	<p><u>Gibson Dunn Comment:</u></p> <ul style="list-style-type: none"> Many companies already include disclosure of the impact of material governmental regulations. Companies will need to consider whether regulatory issues are better addressed in the description of their business or in their risk factors, or whether specific regulatory matters should be addressed in both. As addressed earlier in this client alert, companies should focus on any human capital resources, objectives or measures that are material to them as a whole. 	
<p><u>Item 103</u></p>	<ul style="list-style-type: none"> \$100,000 threshold for disclosure of environmental proceedings involving monetary sanctions and in which the government is a party. 	<ul style="list-style-type: none"> Potential monetary sanctions threshold is raised to \$300,000. Alternatively, a registrant is allowed to set its own disclosure threshold, provided that the threshold cannot exceed the lesser of \$1 million or 1% of current assets, and the registrant must disclose the threshold in each annual and current report. Specifically provides that information about material legal proceedings can be provided by including hyperlinks or cross-references to legal proceedings disclosure located elsewhere in the document in order to avoid duplicative disclosure.
	<p><u>Gibson Dunn Comment:</u></p> <ul style="list-style-type: none"> Many companies already cross-reference or incorporate by reference disclosures that appear in their financial footnotes and/or MD&A. The new rules may lead companies to also include an internal hyperlink. Interpretive guidance may be required to confirm whether disclosure of an alternative dollar threshold for environmental proceedings must be disclosed even when companies have no such proceedings to report, or only when a proceeding involves sanctions exceeding the \$300,000 threshold. Disclosing the dollar amount of a company-determined materiality threshold is not currently a common practice. 	
<p><u>Item 105</u></p>	<ul style="list-style-type: none"> “Most significant” risk factors must be disclosed. 	<ul style="list-style-type: none"> Risk factors are required to be organized under relevant headings, with any risk factors that may generally apply to an investment in securities disclosed at the end of the risk factor section under the caption “General Risk Factors.” Only “material” factors are required to be disclosed. If the Risk Factor section exceeds 15 pages, a maximum two page “summary risk factor disclosure” is required.

Gibson Dunn Comment:

- Companies should confirm that their risk factor subcaptions adequately describe the specific risks addressed, and that their risk factors “concisely explain” how each risk affects the company.
- Many companies already include summaries of their risk factors in their forward-looking statement disclaimers or in the prospectus summary for registration statements. Companies involved in numerous, complex, or highly regulated businesses, as well as those that may be exposed to class action securities litigation, may determine that it is appropriate to include more than 15 pages of risk factors, notwithstanding the additional disclosures that will be triggered.

ANNEX A

Comparison of Regulation S-K Text

[See Attached]

§229.101 (Item 101) Description of business.

(a) *General development of business.* Describe the general development of the business of the registrant, its subsidiaries, and any predecessor(s) ~~during the past five years, or such shorter period as the registrant may have been engaged in business. Information shall be disclosed for earlier periods if material to an understanding of the general development of the business.~~

(1) In describing developments, ~~information shall be given as to matters such as the following: the year in which the registrant was organized and its form of organization; only information material to an understanding of the general development of the business is required. Disclosure may include, but should not be limited to, the following topics:~~

(i) Any material changes to a previously disclosed business strategy;

~~(ii) The~~ The nature and ~~results-effects~~ of any material bankruptcy, receivership, or any similar ~~proceedings-proceeding~~ with respect to the registrant or any of its significant subsidiaries;

~~(iii) The~~ The nature and ~~results-effects~~ of any ~~other~~ material reclassification, merger or consolidation of the registrant or any of its significant subsidiaries; and

~~(iv) The~~ The acquisition or disposition of any material amount of assets otherwise than in the ordinary course of business; ~~and any material changes in the mode of conducting the business.~~

(2) Notwithstanding the provisions of §230.411(b) or §240.12b-23(a) of this chapter, as applicable, a registrant may only forgo providing a full discussion of the general development of its business for a filing other than an initial registration statement if it provides an update to the general development of its business, disclosing all of the material developments that have occurred since the most recent registration statement or report that includes a full discussion of the general development of its business. In addition, the registrant must incorporate by reference, and include one active hyperlink to one registration statement or report that includes, the full discussion of the general development of the registrant's business.

~~(23)~~ Registrants:

(i) Filing a registration statement on Form S-1 (§239.11 of this chapter) under the Securities Act or on Form 10 (§249.210 of this chapter) under the Exchange Act;

(ii) Not subject to the reporting requirements of section 13(a) or 15(d) of the Exchange Act immediately before the filing of such registration statement; and

(iii) That (including predecessors) have not received revenue from operations during each of the three fiscal years immediately before the filing of such registration statement, shall provide the following information:

(A) If the registration statement is filed prior to the end of the registrant's second fiscal quarter, a description of the registrant's plan of operation for the remainder of the fiscal year; or

(B) If the registration statement is filed subsequent to the end of the registrant's second fiscal quarter, a description of the registrant's plan of operation for the remainder of the fiscal year and for

the first six months of the next fiscal year. If such information is not available, the reasons for its not being available shall be stated. Disclosure relating to any plan shall include such matters as:

(1) In the case of a registration statement on Form S-1, a statement in narrative form indicating the registrant's opinion as to the period of time that the proceeds from the offering will satisfy cash requirements and whether in the next six months it will be necessary to raise additional funds to meet the expenditures required for operating the business of the registrant; the specific reasons for such opinion shall be set forth and categories of expenditures and sources of cash resources shall be identified; however, amounts of expenditures and cash resources need not be provided; in addition, if the narrative statement is based on a cash budget, such budget shall be furnished to the Commission as supplemental information, but not as part of the registration statement;

(2) An explanation of material product research and development to be performed during the period covered in the plan;

(3) Any anticipated material acquisition of plant and equipment and the capacity thereof;

(4) Any anticipated material changes in number of employees in the various departments such as research and development, production, sales or administration; and

(5) Other material areas which may be peculiar to the registrant's business.

(b) [Reserved]

(c) ~~Narrative description~~ Description of business. (1) Describe the business done and intended to be done by the registrant and its subsidiaries, focusing upon the registrant's dominant segment or each reportable segment about which financial information is presented in the financial statements. ~~To the extent~~ When describing each segment, only information material to an understanding of the ~~registrant's~~ business taken as a whole, ~~the description of each such segment shall~~ is required. Disclosure may include, but should not be limited to, the information specified in paragraphs (c)(1)-(i) through (xv) of this section. ~~The matters specified in paragraphs (c)(1) (xi) through (xiii) of this section shall be discussed with respect to the registrant's business in general; where material, the segments to which these matters are significant shall be identified.~~

(i) Revenue-generating activities, products and/or services, and any dependence on revenue-generating activities, key products, services, product families or customers, including governmental customers;

(ii) Status of development efforts for new or enhanced products, trends in market demand and competitive conditions;

~~(i) The principal products produced and services rendered by the registrant in the segment and the principal markets for, and methods of distribution of, the segment's principal products and services. In addition, state for each of the last three fiscal years the amount or percentage of total revenue contributed by any class of similar products or services which accounted for 10 percent or more of consolidated revenue in any of the last three fiscal years or 15 percent or more of consolidated revenue, if total revenue did not exceed \$50,000,000 during any of such fiscal years.~~

~~(ii) A description of the status of a product or segment (e.g. whether in the planning stage, whether prototypes exist, the degree to which product design has progressed or whether further engineering is necessary), if there has been a public announcement of, or if the registrant otherwise~~

~~has made public information about, a new product or segment that would require the investment of a material amount of the assets of the registrant or that otherwise is material. This paragraph is not intended to require disclosure of otherwise nonpublic corporate information the disclosure of which would affect adversely the registrant's competitive position.~~

(iii) Resources material to a registrant's business, such as:

~~(iiiA) The sources~~ Sources and availability of raw materials; and

~~(ivB) The importance to the segment and the~~ The duration and effect of all patents, trademarks, licenses, franchises, and concessions held;:-

~~(v) The extent to which the business of the segment is or may be seasonal.~~

~~(vi) The practices of the registrant and the industry (respective industries) relating to working capital items (e.g., where the registrant is required to carry significant amounts of inventory to meet rapid delivery requirements of customers or to assure itself of a continuous allotment of goods from suppliers; where the registrant provides rights to return merchandise; or where the registrant has provided extended payment terms to customers).~~

~~(vii) The dependence of the segment upon a single customer, or a few customers, the loss of any one or more of which would have a material adverse effect on the segment. The name of any customer and its relationship, if any, with the registrant or its subsidiaries shall be disclosed if sales to the customer by one or more segments are made in an aggregate amount equal to 10 percent or more of the registrant's consolidated revenues and the loss of such customer would have a material adverse effect on the registrant and its subsidiaries taken as a whole. The names of other customers may be included, unless in the particular case the effect of including the names would be misleading. For purposes of this paragraph, a group of customers under common control or customers that are affiliates of each other shall be regarded as a single customer.~~

~~(viii) The dollar amount of backlog orders believed to be firm, as of a recent date and as of a comparable date in the preceding fiscal year, together with an indication of the portion thereof not reasonably expected to be filled within the current fiscal year, and seasonal or other material aspects of the backlog. (There may be included as firm orders government orders that are firm but not yet funded and contracts awarded but not yet signed, provided an appropriate statement is added to explain the nature of such orders and the amount thereof. The portion of orders already included in sales or operating revenues on the basis of percentage of completion or program accounting shall be excluded.)~~

~~(ixiv) A description of any material portion of the business that may be subject to renegotiation of profits or termination of contracts or subcontracts at the election of the Government;~~ and

(v) The extent to which the business is or may be seasonal.

~~(x) Competitive conditions in the business involved including, where material, the identity of the particular markets in which the registrant competes, an estimate of the number of competitors and the registrant's competitive position, if known or reasonably available to the registrant. Separate consideration shall be given to the principal products or services or classes of products or services of the segment, if any. Generally, the names of competitors need not be disclosed. The registrant may include such names, unless in the particular case the effect of including the names would be misleading. Where, however, the registrant knows or has reason to know that one or a small number of competitors is dominant in the industry it shall be identified. The principal methods of competition~~

~~(e.g., price, service, warranty or product performance) shall be identified, and positive and negative factors pertaining to the competitive position of the registrant, to the extent that they exist, shall be explained if known or reasonably available to the registrant.~~

~~(xi) [Reserved]~~

~~(xii) Appropriate disclosure also shall be made as to the material effects that compliance with Federal, State and local provisions which have been enacted or adopted regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries. The registrant shall disclose any material estimated capital expenditures for environmental control facilities for the remainder of its current fiscal year and its succeeding fiscal year and for such further periods as the registrant may deem materials.~~

~~(xiii) The number of persons employed by the registrant.~~

(2) Discuss the information specified in paragraphs (c)(2)(i) and (ii) of this section with respect to, and to the extent material to an understanding of, the registrant's business taken as a whole, except that, if the information is material to a particular segment, you should additionally identify that segment.

(i) The material effects that compliance with government regulations, including environmental regulations, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries, including the estimated capital expenditures for environmental control facilities for the current fiscal year and any other material subsequent period; and

(ii) A description of the registrant's human capital resources, including the number of persons employed by the registrant, and any human capital measures or objectives that the registrant focuses on in managing the business (such as, depending on the nature of the registrant's business and workforce, measures or objectives that address the development, attraction and retention of personnel).

(d) [Reserved]

(e) *Available information.* Disclose the information in paragraphs (e)(1), (e)(2) and (e)(3) of this section in any registration statement you file under the Securities Act (15 U.S.C. 77a *et seq.*), and disclose the information in paragraph (e)(3) of this section in your annual report on Form 10-K (§249.310 of this chapter). Further disclose the information in paragraph (e)(4) of this section if you are an accelerated filer or a large accelerated filer (as defined in §240.12b-2 of this chapter) filing an annual report on Form 10-K (§249.310 of this chapter):

(1) Whether you file reports with the Securities and Exchange Commission. If you are a reporting company, identify the reports and other information you file with the SEC.

(2) State that the SEC maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC and state the address of that site (<http://www.sec.gov>).

(3) Disclose your internet address, if you have one.

(4)(i) Whether you make available free of charge on or through your Internet website, if you have one, your annual report on Form 10-K, quarterly reports on Form 10-Q (§249.308a of this chapter), current reports on Form 8-K (§249.308 of this chapter), and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act (15 U.S.C. 78m(a) or 78o(d)) as soon as reasonably practicable after you electronically file such material with, or furnish it to, the SEC;

(ii) If you do not make your filings available in this manner, the reasons you do not do so (including, where applicable, that you do not have an Internet website); and

(iii) If you do not make your filings available in this manner, whether you voluntarily will provide electronic or paper copies of your filings free of charge upon request.

(f) *Reports to security holders.* Disclose the following information in any registration statement you file under the Securities Act:

(1) If the SEC's proxy rules or regulations, or stock exchange requirements, do not require you to send an annual report to security holders or to holders of American depository receipts, describe briefly the nature and frequency of reports that you will give to security holders. Specify whether the reports that you give will contain financial information that has been examined and reported on, with an opinion expressed "by" an independent public or certified public accountant.

(2) For a foreign private issuer, if the report will not contain financial information prepared in accordance with U.S. generally accepted accounting principles, you must state whether the report will include a reconciliation of this information with U.S. generally accepted accounting principles.

(g) *Enforceability of civil liabilities against foreign persons.* Disclose the following if you are a foreign private issuer filing a registration statement under the Securities Act:

(1) Whether or not investors may bring actions under the civil liability provisions of the U.S. Federal securities laws against the foreign private issuer, any of its officers and directors who are residents of a foreign country, any underwriters or experts named in the registration statement that are residents of a foreign country, and whether investors may enforce these civil liability provisions when the assets of the issuer or these other persons are located outside of the United States. The disclosure must address the following matters:

(i) The investor's ability to effect service of process within the United States on the foreign private issuer or any person;

(ii) The investor's ability to enforce judgments obtained in U.S. courts against foreign persons based upon the civil liability provisions of the U.S. Federal securities laws;

(iii) The investor's ability to enforce, in an appropriate foreign court, judgments of U.S. courts based upon the civil liability provisions of the U.S. Federal securities laws; and

(iv) The investor's ability to bring an original action in an appropriate foreign court to enforce liabilities against the foreign private issuer or any person based upon the U.S. Federal securities laws.

(2) If you provide this disclosure based on an opinion of counsel, name counsel in the prospectus and file as an exhibit to the registration statement a signed consent of counsel to the use of its name and opinion.

(h) *Smaller reporting companies.* A smaller reporting company, as defined by §229.10(f)(1), may satisfy its obligations under this Item by describing the development of its business ~~during the last three years~~ pursuant to this paragraph (h). In describing developments under paragraphs (h)(1) through (3), information should be provided for the period of time that is material to an understanding of the general development of the business. Notwithstanding the provisions of §230.411(b) or §240.12b-23(a) of this chapter as applicable, a smaller reporting company may only forgo providing a full discussion of the general development of its business for a filing other than an initial registration statement if it provides an update to the general development of its business disclosing all of the material developments that have occurred since the most recent registration statement or report that includes a full discussion of the general development of its business. In addition, the smaller reporting company must incorporate by reference, and include one active hyperlink to one registration statement or report that includes, the full discussion of the general development of the registrant's business. If the smaller reporting company has not been in business for three years, ~~give~~ provide the same information for predecessor(s) of the smaller reporting company if there are any. This business development description should include:

(1) Form and year of organization;

(2) Any bankruptcy, receivership or similar proceeding; and

(3) Any material reclassification, merger, consolidation, or purchase or sale of a significant amount of assets not in the ordinary course of business.

(4) *Business of the smaller reporting company.* Briefly describe the business and include, to the extent material to an understanding of the smaller reporting company:

(i) Principal products or services and their markets;

(ii) Distribution methods of the products or services;

(iii) Status of any publicly announced new product or service;

(iv) Competitive business conditions and the smaller reporting company's competitive position in the industry and methods of competition;

(v) Sources and availability of raw materials and the names of principal suppliers;

(vi) Dependence on one or a few major customers;

(vii) Patents, trademarks, licenses, franchises, concessions, royalty agreements or labor contracts, including duration;

(viii) Need for any government approval of principal products or services. If government approval is necessary and the smaller reporting company has not yet received that approval, discuss the status of the approval within the government approval process;

(ix) Effect of existing or probable governmental regulations on the business;

(x) [Reserved]

(xi) Costs and effects of compliance with environmental laws (federal, state and local); and

(xii) Number of total employees and number of full-time employees.

(5) *Reports to security holders.* Disclose the following in any registration statement you file under the Securities Act of 1933:

(i) If you are not required to deliver an annual report to security holders, whether you will voluntarily send an annual report and whether the report will include audited financial statements;

(ii) Whether you file reports with the Securities and Exchange Commission. If you are a reporting company, identify the reports and other information you file with the Commission; and

(iii) State that the Commission maintains an internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the Commission and state the address of that site (<http://www.sec.gov>). Disclose your internet address, if available.

(6) *Foreign issuers.* Provide the information required by Item 101(g) of Regulation S-K (§229.101(g)).

Instructions to Item 101: 1. In determining what information about the segments is material to an understanding of the registrant's business taken as a whole and therefore required to be disclosed, pursuant to paragraph (c) of this Item, the registrant should take into account both quantitative and qualitative factors such as the significance of the matter to the registrant (e.g., whether a matter with a relatively minor impact on the registrant's business is represented by management to be important to its future profitability), the pervasiveness of the matter (e.g., whether it affects or may affect numerous items in the segment information), and the impact of the matter (e.g., whether it distorts the trends reflected in the segment information). Situations may arise when information should be disclosed about a segment, although the information in quantitative terms may not appear significant to the registrant's business taken as a whole.

2. Base the determination of whether information about segments is required for a particular year upon an evaluation of interperiod comparability. For instance, interperiod comparability would require a registrant to report segment information in the current period even if not material under the criteria for reportability of FASB ASC Topic 280, *Segment Reporting*, if a segment has been significant in the immediately preceding period and the registrant expects it to be significant in the future.

3. The Commission, upon written request of the registrant and where consistent with the protection of investors, may permit the omission of any of the information required by this Item or the furnishing in substitution thereof of appropriate information of comparable character.

* * * *

§229.103 (Item 103) Legal proceedings.

(a) Describe briefly any material pending legal proceedings, other than ordinary routine litigation incidental to the business, to which the registrant or any of its subsidiaries is a party or of which any of their property is the subject. Include the name of the court or agency in which the proceedings are pending, the date instituted, the principal parties thereto, a description of the factual basis alleged to underlie the ~~proceeding~~ proceedings and the relief sought. Include similar information as to any such proceedings known to be contemplated by governmental authorities.

Information may be provided by hyperlink or cross-reference to legal proceedings disclosure elsewhere in the document, such as in Management's Discussion & Analysis (MD&A), Risk Factors and notes to the financial statements.

(b) No information need be given under this section for proceedings:

(1) That involve negligence or other claims or actions if

~~Instructions to Item 103: 1. If the business ordinarily results in such claims or actions for negligence or other claims, no such action or, unless the claim or action need be described unless it~~ departs from the normal kind of such claims or actions; or.

~~(2) 2. No information need be given with respect to any proceeding t~~hat involves primarily a claim for damages if the amount involved, exclusive of interest and costs, does not exceed 10 percent of the current assets of the registrant and its subsidiaries on a consolidated basis. However, if any proceeding presents in large degree the same legal ~~and or~~ factual issues as other proceedings pending or known to be contemplated, the amount involved in such other proceedings shall be included in computing such percentage.

~~(c)3.~~ Notwithstanding paragraph (b) of this section~~Instructions 1 and 2,~~ disclosure under this section shall include, but shall not be limited to:

~~(1) a~~Any material bankruptcy, receivership, or similar proceeding with respect to the registrant or any of its significant subsidiaries ~~shall be described.;~~

~~(2)4.~~ Any material proceedings to which any director, officer or affiliate of the registrant, any owner of record or beneficially of more than five percent of any class of voting securities of the registrant, or any associate of any such director, officer, affiliate of the registrant, or security holder is a party adverse to the registrant or any of its subsidiaries or has a material interest adverse to the registrant or any of its subsidiaries ~~also shall be described.;~~

~~(3)5. Notwithstanding the foregoing, an a~~Administrative or judicial proceedings (including, ~~for purposes of A and B of this Instruction,~~ proceedings which present in large degree the same issues) arising under any Federal, State, or local provisions that have been enacted or adopted regulating the discharge of materials into the environment or primarily for the purpose of protecting the environment. Such proceedings shall not be deemed "ordinary routine litigation incidental to the business" and shall be described if:

~~(i)A.~~ Such proceeding is material to the business or financial condition of the registrant;

~~(ii)B.~~ Such proceeding involves primarily a claim for damages, or involves potential monetary sanctions, capital expenditures, deferred charges or charges to income and the amount involved, exclusive of interest and costs, exceeds 10 percent of the current assets of the registrant and its subsidiaries on a consolidated basis; or

~~(iii)C.~~ A governmental authority is a party to such proceeding and such proceeding involves potential monetary sanctions, unless the registrant reasonably believes that such proceeding will result in no monetary sanctions, or in monetary sanctions, exclusive of interest and costs, of less than \$~~100~~300,000 or, at the election of the registrant, such other threshold that (A) the registrant determines is reasonably designed to result in disclosure of any such proceeding that is material to the business or financial condition is disclosed, (B) the registrant discloses (including any change

thereto) in each annual and quarterly report, and (C) does not exceed the lesser of \$1 million or one percent of the current assets of the registrant and its subsidiaries on a consolidated basis; provided, however, that such proceedings ~~which that~~ are similar in nature may be grouped and described generically.

* * * *

§229.105 (Item 105) Risk factors.

(a) Where appropriate, provide under the caption “Risk Factors” a discussion of the ~~most significant~~ material factors that make an investment in the registrant or offering speculative or risky. This discussion must be ~~concise and~~ organized logically with relevant headings and each risk factor should be set forth under a subcaption that adequately describes the risk. The presentation of ~~Do not present~~ risks that could apply generically to any registrant or any offering is discouraged, but to the extent generic risk factors are presented, disclose them at the end of the risk factor section under the caption “General Risk Factors.”

(b) ~~Explain~~ Concisely explain how ~~the~~ each risk affects the registrant or the securities being offered. ~~Set forth each risk factor under a subcaption that adequately describes the risk. If the discussion is longer than 15 pages, include in the forepart of the prospectus or annual report, as applicable, a series of concise, bulleted or numbered statements that is no more than two pages summarizing the principal factors that make an investment in the registrant or offering speculative or risky.~~ If the risk factor discussion is included in a registration statement, it must immediately follow the summary section required by §229.503 (Item 503 of Regulation S-K). If you do not include a summary section, the risk factor section must immediately follow the cover page of the prospectus or the pricing information section that immediately follows the cover page. Pricing information means price and price-related information that you may omit from the prospectus in an effective registration statement based on Rule 430A (§230.430A ~~(a)~~) of this chapter). The registrant must furnish this information in plain English. See §230.421(d) of Regulation C of this chapter.



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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