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*SEC Enforcement Focus on COVID-19
Issues and Key Risks*

November 18, 2020

Panelists:

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Michael J. Scanlon
Jason H. Smith

MCLE Certificate Information

- Most participants should anticipate receiving their certificate of attendance via email approximately four weeks following the webcast.
- Virginia Bar Association members should anticipate receiving their certificate of attendance six weeks following the webcast.
- **Please direct all questions regarding MCLE to CLE@gibsondunn.com.**

Panelists



[Richard W. Grime](#) is co-chair of Gibson Dunn's Securities Enforcement Practice Group. Mr. Grime's practice focuses on representing companies and individuals in corruption, accounting fraud, and securities enforcement matters before the SEC and the DOJ. Prior to joining the firm, Mr. Grime was Assistant Director in the Division of Enforcement at the SEC, where he supervised the filing of over 70 enforcement actions covering a wide range of the Commission's activities, including the first FCPA case involving SEC penalties for violations of a prior Commission order, numerous financial fraud cases, and multiple insider trading and Ponzi-scheme enforcement actions.



[Monica K. Loseman](#) is co-chair of Gibson, Dunn's Securities Litigation Practice Group and is a partner in the Denver office. Ms. Loseman has substantial experience in complex corporate and securities enforcement matters and civil litigation. Her practice includes a focus on financial reporting, accounting and related investigations and accountant defense. Ms. Loseman's trial experience largely focused on accounting and financial reporting and corporate governance matters, including three trials before SEC administrative law judges, several bench and jury trials, and private arbitrations. Ms. Loseman also conducts independent investigations involving allegations of corporate fraud and issues relating to financial reporting, accounting, internal controls.



[Michael J. Scanlon](#) is a partner in the Washington, D.C. office, where he is a member of the Firm's Securities Regulation and Corporate Governance, and Securities Enforcement Practice Groups. Mr. Scanlon has an extensive practice representing U.S. and foreign public company and audit firm clients on regulatory, corporate governance, and enforcement matters. He advises corporate clients on SEC compliance and disclosure issues, the Sarbanes-Oxley Act, and corporate governance best practices, with a particular focus on financial reporting matters.



[Jason H. Smith](#) is a senior associate in the Washington, D.C. office where, he is a member of the White Collar Defense and Investigations Practice Group and focuses primarily on white collar defense, corporate compliance, and securities enforcement. Mr. Smith has particular experience representing multinational corporate clients in government investigations, including before the Department of Justice, Securities and Exchange Commission, and other regulatory and enforcement agencies.

Agenda

- 1. SEC Enforcement Division Overview**
- 2. 2020 Enforcement Trends and the Impact of COVID-19**
- 3. What to Watch in 2021 and Beyond**
- 4. Key Areas of Accounting Risk**
- 5. Key Areas of Disclosure Risk**

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SEC Enforcement Division Overview

SEC Enforcement Division

An Introduction

- Organization of the Commission:

- 1 Chairperson and 4 Commissioners
- 5 Divisions: Enforcement, Corporation Finance, Economic and Risk Analysis, Investment Management, and Trading and Markets
- Additional components include Office of Chief Accountant, Office of Compliance Inspections and Examinations, and Office of the Whistleblower.



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Chairman



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Peirce
Commissioner
since 2018
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Elad L.
Risman
Commissioner
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Allison
Herren Lee
Commissioner
since 2019
Term exp. 2022



Caroline A.
Crenshaw
Commissioner
since 2020
Term exp. 2024

SEC Enforcement Division

An Introduction

- Enforcement Division is SEC's largest unit with more than 1,350 investigators, accountants, trial attorneys, and other professionals
- Investigates potential securities law violations
- Prosecution of civil actions in federal court or administrative proceedings
- DC headquarters, with enforcement attorneys across 11 Regional Offices (e.g., Atlanta, Miami, NYC, Los Angeles, Salt Lake City)
- Currently led by Stephanie Avakian



SEC Enforcement Division

Supporting Units

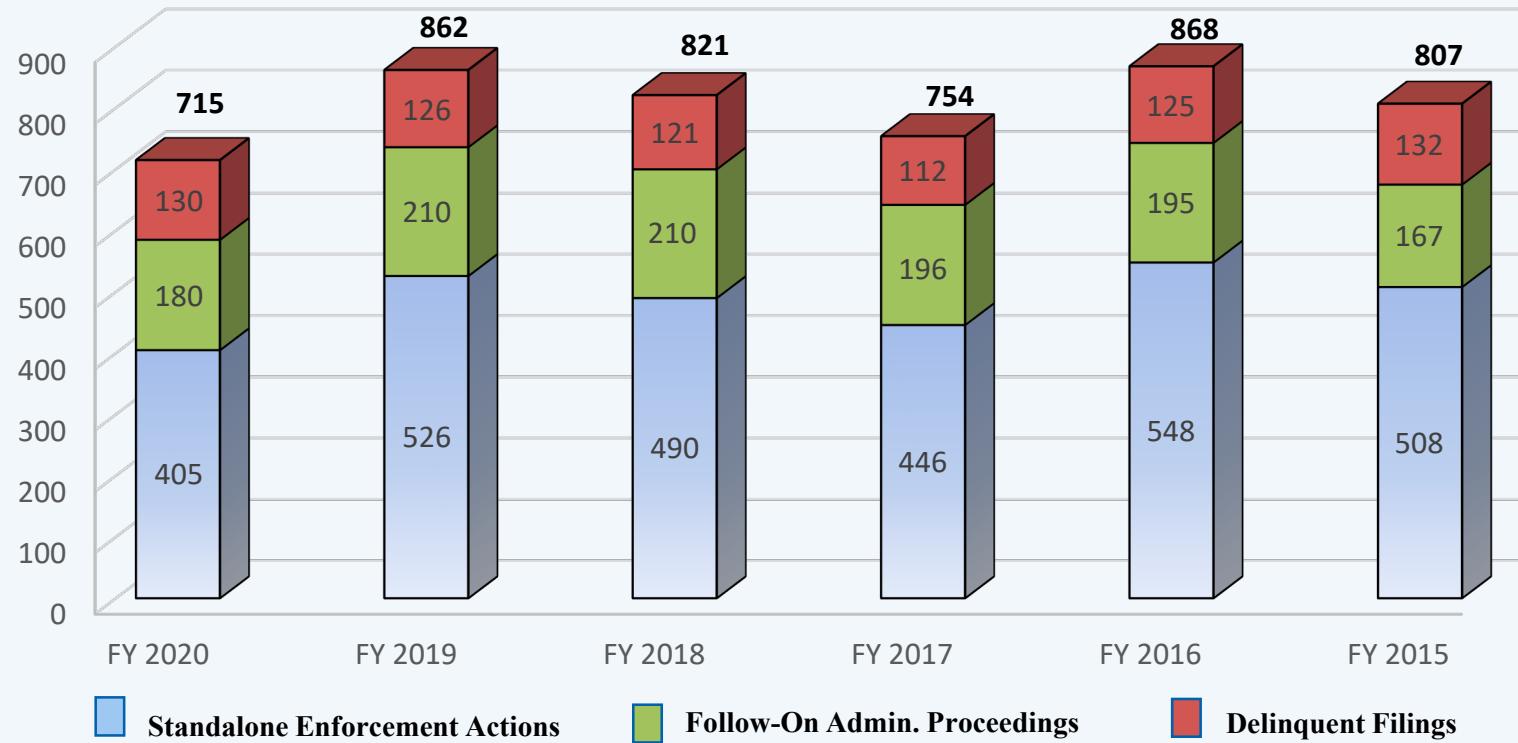
Unit	Role
Asset Management	<ul style="list-style-type: none">Focused on misconduct by investment advisors, investment companies, private equity funds, and hedge funds
Complex Financial Instruments	<ul style="list-style-type: none">Focused on misconduct involving complex derivatives and financial products such as collateralized debt obligations, credit defaults swaps, and securitized products
FCPA	<ul style="list-style-type: none">Responsible for investigating violations of the Foreign Corrupt Practices Act
Market Abuse	<ul style="list-style-type: none">Focused on investigations involving large-scale market abuses and complex manipulation schemes by institutional traders and market professionals
Municipal Securities and Public Pensions	<ul style="list-style-type: none">Focused on wrongdoing in the large municipal securities market and in connection with public pension funds
Cyber	<ul style="list-style-type: none">Targets cyber-related misconduct such as market manipulation schemes through social media, hacking non-public information, and threats to brokerage accounts
Retail Strategy	<ul style="list-style-type: none">Focused on identifying misconduct affecting retail investors

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2020 Enforcement Trends and the Impact of COVID-19

FY 2020 Enforcement Trends

Total Actions and Monetary Remedies

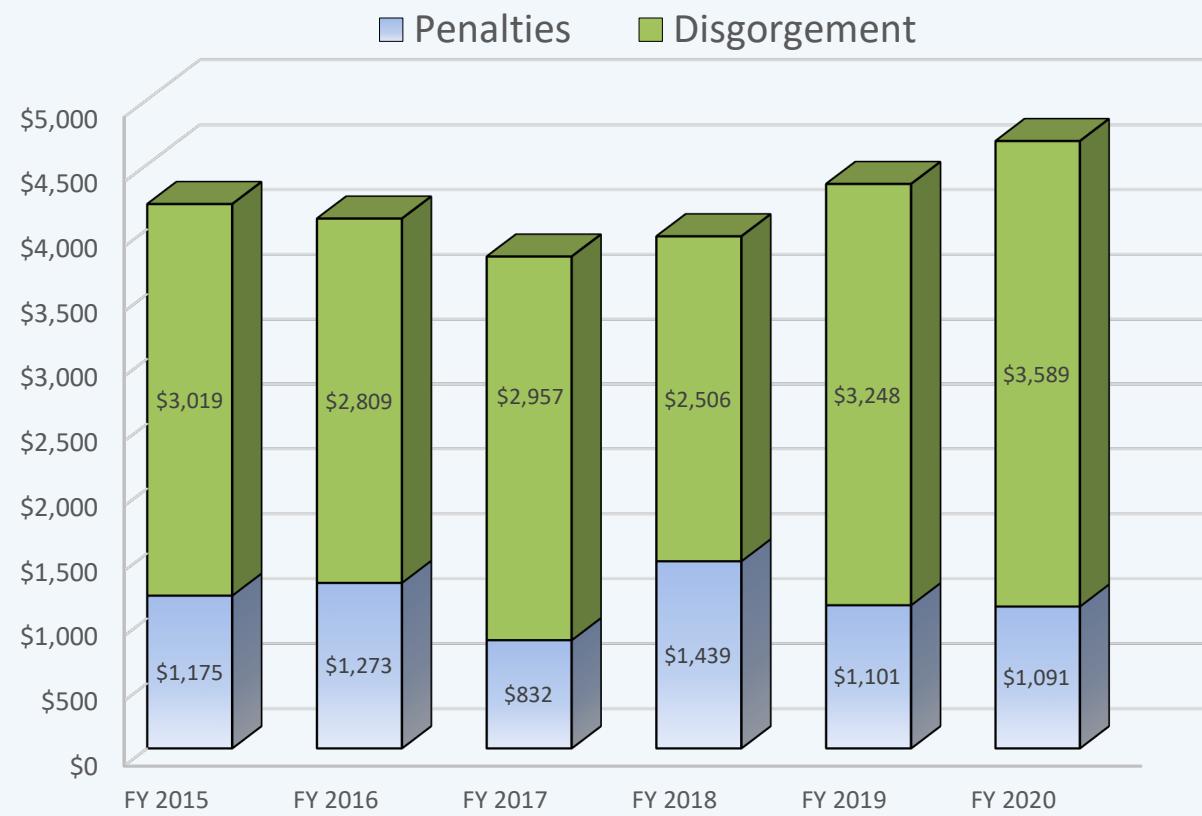


- The SEC filed 715 enforcement actions in FY 2020, a 17% decrease from FY 2019.
 - 492 of these cases were brought after teleworking was instituted in mid-March.
 - Over 40% of standalone matters were filed as litigated actions, a 10% increase from FY 2019.
 - In FY 2020, the SEC opened 640 new matters, of which 150 are coronavirus related.

FY 2020 Enforcement Trends

Total Actions and Monetary Remedies

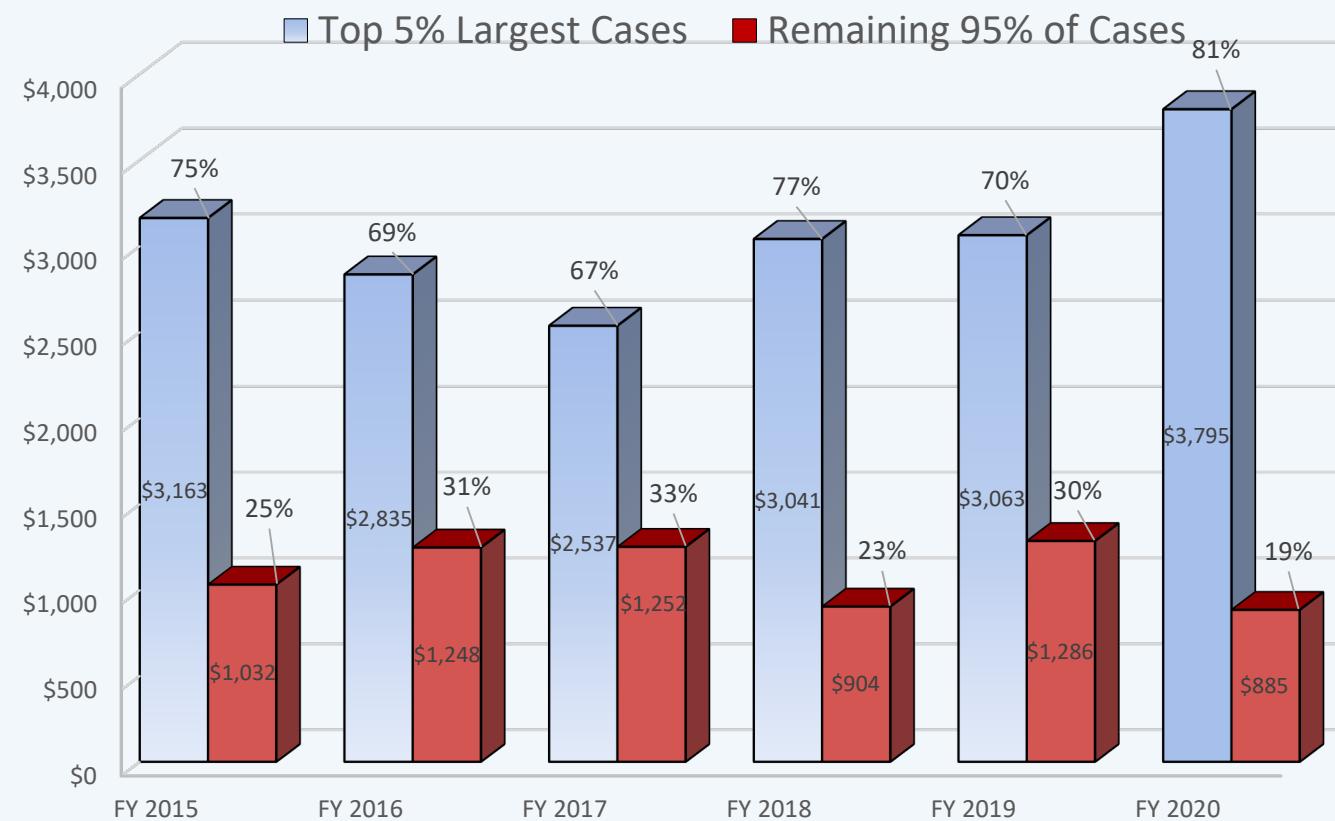
Despite a decrease in enforcement actions, there was a **7.6% increase** in monetary remedies compared with FY 2019.



FY 2020 Enforcement Trends

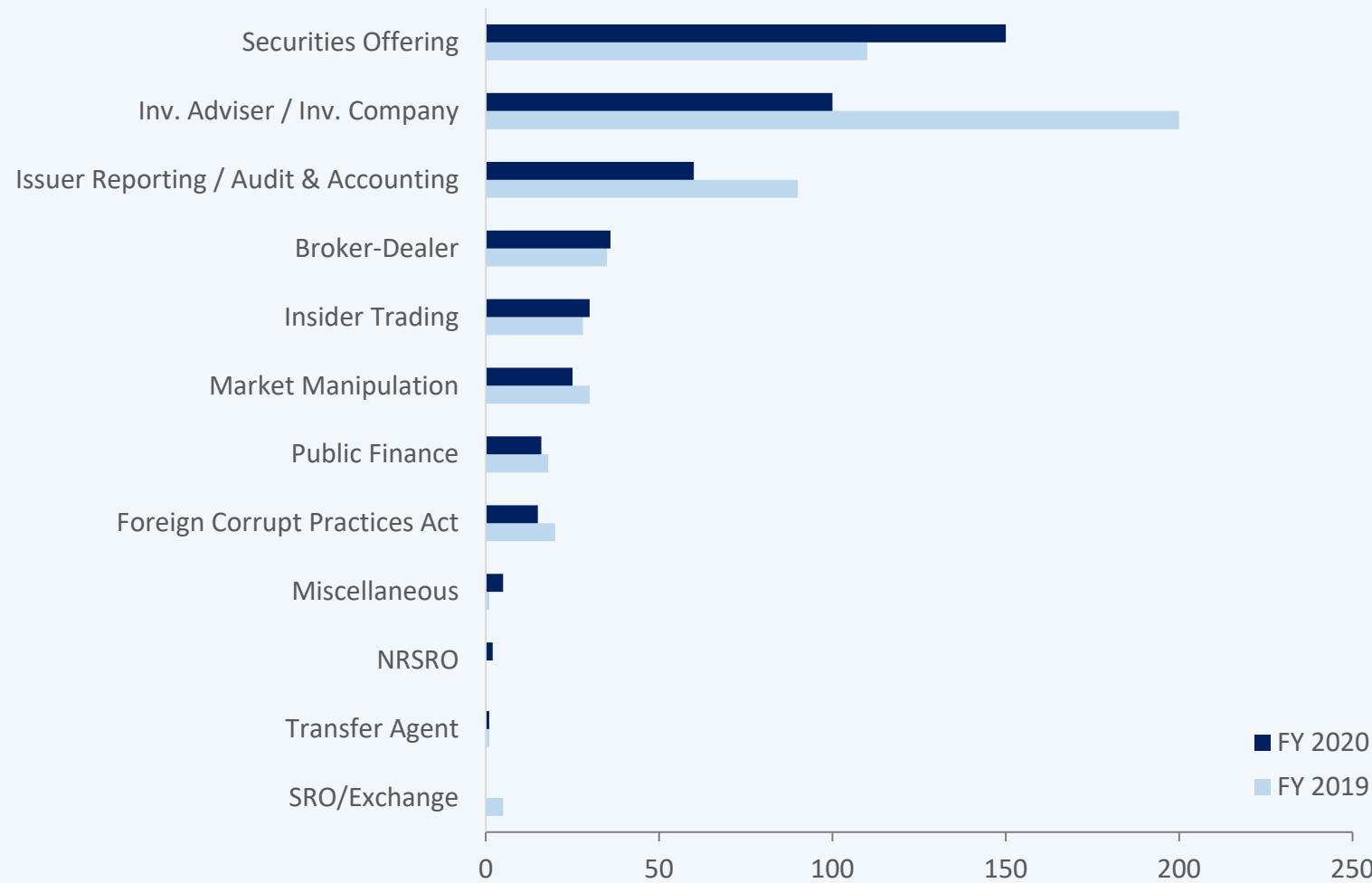
Total Actions and Monetary Remedies

The top 5% of cases with the largest financial remedies represented a record-setting **81%** of all financial remedies in FY 2020.



FY 2020 Enforcement Trends

Types of Cases



FY 2020 Enforcement Trends

COVID-19 Enforcement Actions



- Pandemic-related enforcement actions have thus far focused on alleged misconduct of companies that attempted to profit directly from the coronavirus. For example:
 - *Praxsyn Corp.* (April 28, 2020)
 - Trading in the company's stock had already been halted by the SEC weeks before the enforcement action.
 - The company allegedly issued a press release stating that it was negotiating the sale of millions of N95 masks and “evaluating multiple orders and vetting various suppliers in order to guarantee a supply chain that can deliver millions of masks on a timely schedule.”
 - The company allegedly issued a second press release claiming it had a large number of N95 masks on hand and had created a “direct pipeline from manufacturers and suppliers to buyers” of the masks.
 - According to the SEC, the company allegedly never had any masks in its possession or any orders for masks.

FY 2020 Enforcement Trends

COVID-19 Enforcement Actions



- *Applied Biosciences Corp.* (May 14, 2020)
 - The SEC had halted trading on the company's stock weeks before filing an enforcement action.
 - The company allegedly issued a press release stating that it had formulated its own hand sanitizing blends according to CDC guidelines.
 - The company allegedly issued a second press release stating that it had started shipping a COVID-19 home testing kit that could provide results in only 15 minutes.
 - The stock price increased nearly 80% after publication of these press releases.
 - The SEC alleged that the company never produced its own hand sanitizer, which was instead being sourced from a third-party manufacturer.
 - According to the SEC, shipping of the test kits had never started, and the company had merely entered into an agreement to purchase test kits from an essential oils company that had sourced the test kits from China.

FY 2020 Enforcement Trends

COVID-19 Enforcement Actions



- *Turbo Global Partners Inc.* (May 14, 2020)
 - The company allegedly issued a press release touting a “public-private partnership” with government entities in which it would be the exclusive distributor of thermal scanning equipment designed to detect fevers and recognize faces.
 - The company allegedly issued a second press release claiming that it had been contacted by the governor’s offices for all 50 states inquiring into the equipment.
 - The stock price jumped by as much as 300% after the press releases.
 - According to the SEC, the company never entered into a public-private partnership.
 - The SEC alleges that the equipment had no face recognition abilities.
 - According to the SEC, “contact” with the governor’s offices consisted only of unsolicited emails and faxes from the company.

FY 2020 Enforcement Trends

Adapting Enforcement Practices

- The Enforcement Division is adapting its fact-gathering techniques by:
 - Issuing interrogatory-like requests to parties under investigation;
 - Seeking documents and other information from third parties such as auditors;
 - Receiving attorney proffers at earlier points in the investigation to narrow follow-up requests; and
 - Holding testimony, depositions, and Wells meetings by videoconference.
- The SEC has pushed for testimony by videoconference but has shown some flexibility with the ground rules. For instance, Enforcement attorneys have:
 - Shown greater flexibility with sharing documents in advance;
 - Been allowing breaks at shorter intervals; and
 - Sometimes allowed for attorney proffers in lieu of testimony.
- For witnesses who refuse to testify remotely, the SEC has considered issuing a Wells notice and later taking a video deposition during litigation.
- In July 2020, the SEC litigated (and won) its first virtual bench trial post-coronavirus.
 - The SEC anticipates more trials in the near future.

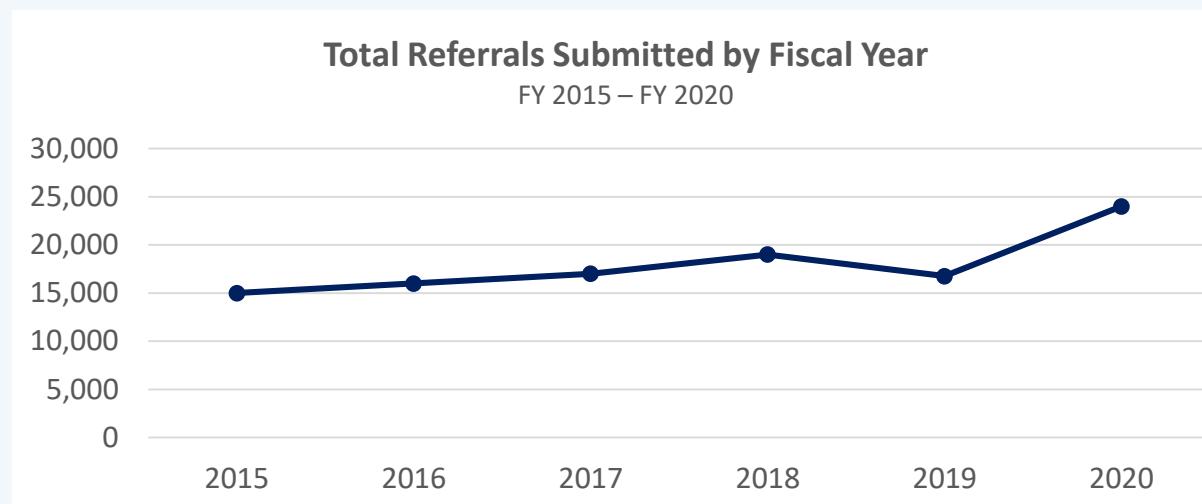
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What to Watch in 2021 and Beyond

What to Watch in 2021 and Beyond

Enforcement Actions and Proceedings

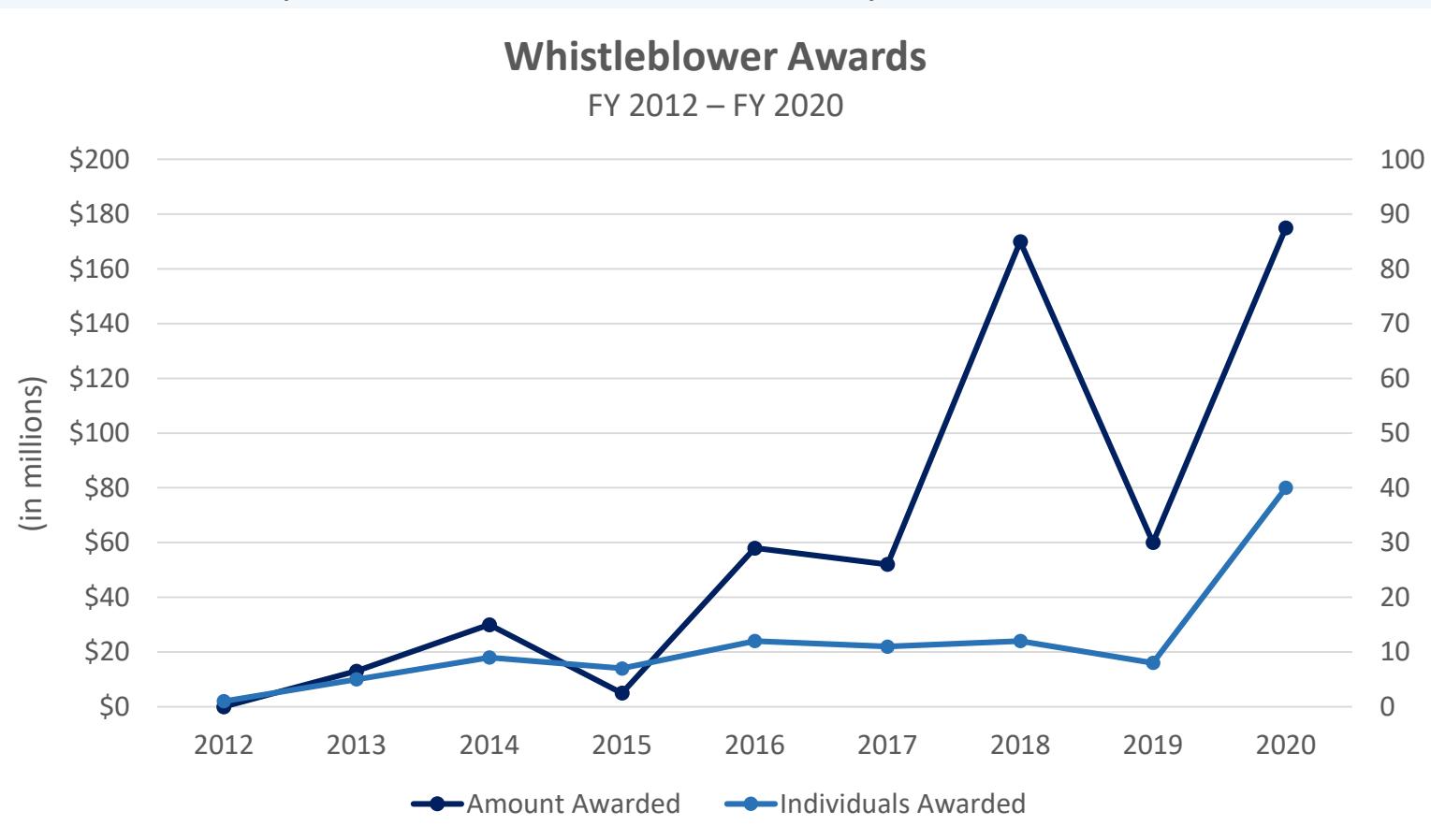
- A future uptick in enforcement actions and proceedings is expected in light of increases in referrals and investigations.
 - 1,181 new inquiries and investigations in FY 2020 versus 1,082 in FY 2019
 - 7% year-over-year increase from mid-March through FY 2020
 - 40% increase in tips and referrals will add to the volume of investigations
 - 23,650 tips and referrals in FY 2020 versus 16,850 in FY 2019
 - 16,000 tips and referrals from mid-March through FY 2020, a 71% year-over-year increase



What to Watch in 2021 and Beyond

Whistleblower Awards

- Record-breaking whistleblower awards, both in amount and frequency, will incentivize more tips that will become the catalyst for future enforcement actions.



What to Watch in 2021 and Beyond

Enforcement Priorities

- In March 2020, the Enforcement Division created the COVID-19 Steering Committee to identify areas of potential misconduct and coordinate the Division's response to COVID-19 related issues.
- The Committee identified five enforcement priorities:
 - *Insider Trading and Market Manipulation*: suspicious market movements attributable to material non-public information
 - *Accounting Fraud*: accounting that inaccurately characterizes preexisting financial statement issues as coronavirus related and disclosures that appear misaligned with peer companies
 - *Asset Management*: asset managers' conduct with respect to valuations, redemption requests, liquidity, disclosures, and conflicts among clients and between clients and the manager
 - *Complex Financial Instruments*: concealed risks associated with complex structured products and how those risks are disclosed to investors
 - *Microcap Fraud*: focus on suspension of trading on securities due to allegedly false or misleading claims related to the coronavirus
- The Enforcement Division has emphasized that these priorities will not detract from the Division's usual diet of non-coronavirus enforcement actions.

What to Expect in 2021 and Beyond

Trends to Watch

- *Enhanced Market Monitoring:* Expect heavier reliance on data analytics, such as the EPS Initiative, to identify potential accounting and disclosure violations.
- *Industry Sweeps:* Expect continued inquiries targeting public companies receiving PPP loans and the impact of COVID-19 on business activities and ability to continue as a going concern.
- *Exams:* Since early March, the SEC has been requesting information from registered investment companies and advisors regarding their COVID-19 preparedness and policies. Registered investment companies and advisors who have received stimulus funds should expect requests regarding their qualifications for, use of, and adequate disclosures regarding stimulus funds.
- *Accounting and Disclosure Fraud Cases:* The Enforcement Division is closely scrutinizing how companies disclose coronavirus-related risks to their business and account for its impact on financials. These investigations are inherently time-consuming and likely will start resulting in enforcement actions in 2021 and beyond.

What to Expect in 2021 and Beyond

Trends to Watch – Insider Trading and Internal Control Violations



- In October 2020, Andeavor agreed to pay a \$20 million civil penalty for alleged internal accounting controls violations under Exchange Act Section 13(b)(2)(B). The SEC alleged that:
 - Andeavor executed stock repurchases while the CEO had privately agreed to an acquisition.
 - The repurchases were executed under a Rule 10b5-1 plan and with the prior approval of the company's legal department, which concluded that the company did not possess material non-public information.
 - At the time the plan was approved, acquisition discussions had been suspended.
 - The Board of Directors authorized the share repurchases.
- The SEC alleged that the legal department used an "abbreviated and informal process" to evaluate the materiality of the acquisition, resulting in a "deficient understanding" of the facts.
- Two Commissioners dissented on the ground that the internal controls provision targets accounting control deficiencies rather than corporate governance issues.



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Key Areas of Accounting Risk

Key Areas of Accounting Risk

Office of Chief Accountant

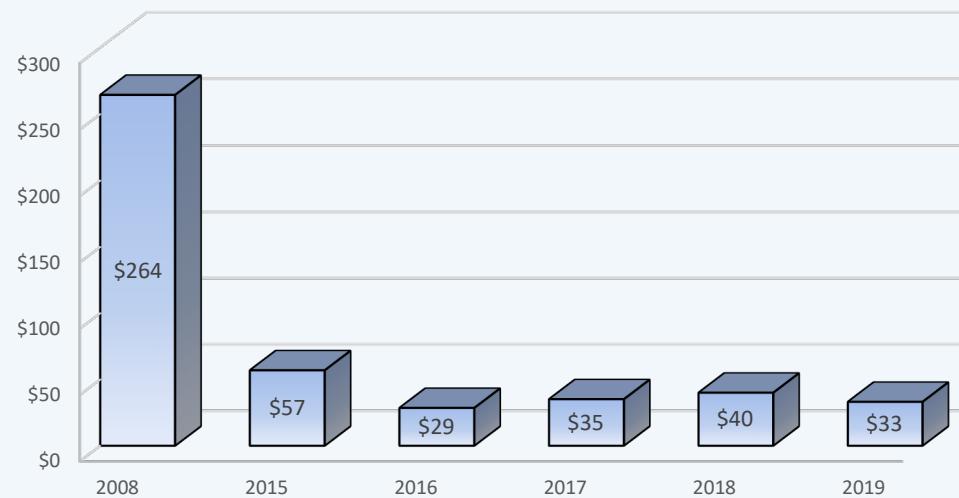
- In April 2020, the Office of the Chief Accountant issued a statement stressing the importance of quality reasoning in areas requiring a high degree of accounting judgment. The statement identified the following accounting topics, among others:
 - Fair value and impairment considerations
 - Leases
 - Debt modifications or restructurings
 - Hedging
 - Revenue recognition
 - Income taxes
 - Going concern
 - Subsequent events
 - Adoption of new accounting standards (e.g., the new credit losses standard)

Key Areas of Accounting Risk

Fair Value and Impairment

- Over the last several years, the SEC has increasingly scrutinized impairment and fair value accounting.
 - Impairment and intangible asset accounting have been among the top 10 most frequently occurring topics in SEC comment letters.
 - Fair value measurement and valuations are among the top 3 most frequently occurring topics in SEC comment letters.
- Based on the impairment rates during the financial crisis, we expect 2020 will see a significant uptick in impairments.

■ Total Goodwill Impairments by U.S. Companies (in billions)



Source: Duff & Phelps LLC. 2019 data only includes 10 largest goodwill impairments reported through Q3 2019

Key Areas of Accounting Risk

Fair Value and Impairment

- Impairment testing consists of comparing the business' fair value against each operating segments' carrying amount, or book value.
 - Entities must run impairment testing at least annually or whenever indicators of impairment arise.
 - If book value exceeds the fair value, then the company must record an impairment.
- Fundamental question in an SEC investigation: Should an impairment have been recorded at an earlier date?
 - No “grace period” to record an impairment
 - Impairments investigated even if stock increases after an announcement
 - Concurrence of independent auditors is not a foolproof protection
- Key areas of scrutiny:
 - *Triggering event:* Did the company ignore or underappreciate circumstances that would call for an impairment test?
 - *Cash-flow projections:* Are aspirational / unattainable cash-flow projections being used? How frequently are cash-flow projections being revised in light of changed circumstances?
 - *Discount rate:* Is the discount rate fully appreciating the implications of COVID-19 and being regularly revisited?

Key Areas of Accounting Risk

Revenue Recognition

- Revenue recognition was the second most frequently appearing topic in SEC comment letters in FY 2020.
- Uncertainty prompted by COVID-19 complicates revenue recognition assessments.

Accounting Concept	COVID-19 Considerations
Assessing the ability to collect the consideration promised	<ul style="list-style-type: none">• Entities should continually reassess customers' ability to make payment and make adjustments to receivables as necessary.• Assessments should consider whether revenue can continue to be recognized on new transactions with customers in similar circumstances.
Not recognizing revenue in excess of what is probable to reverse (i.e., "variable consideration")	<ul style="list-style-type: none">• Negative impacts of the pandemic on estimates of volume discounts, rebates, refunds, and returns may require companies to reassess and update previous estimates.
Accurate measurement of revenue that is recognized over time	<ul style="list-style-type: none">• The pandemic can affect the pattern and period over which to record revenue.• The coronavirus may also hinder access to supplies and labor, which can affect the timing of revenue where inputs are used to measure progress for revenue recognition (e.g., construction projects).

- Entities should continually consider disclosures of the judgments used for revenue recognition.

Key Areas of Accounting Risk

Going Concern

- Going concern considers whether a business can reasonably continue operating for the next 12 months.
- Management and directors must reach a view taking into account all available information.

Areas For SEC Scrutiny	Key Questions to Consider
Strength of Analysis	<ul style="list-style-type: none">• Does the assessment consider overall market and economic conditions, significant drops in demand or customer reductions, changes in government support to the business / industry, supply chain disruptions, geographic or country risks, and limitations on distribution channels?• Does the assessment consider the company's liquidity, including funding restrictions, working capital management and assumptions, and shifts in supplier credit terms or debtor payment cycles?• Does the assessment consider the company's reliance on government assistance or grants and the likelihood of their future termination?
Depth of Analysis / Documentation	<ul style="list-style-type: none">• Is management's analysis sufficiently detailed to enable directors to reach an informed view and based on a fulsome assessment of COVID-19 risks?• Is there sufficient documentation showing the basis of management's assessment and challenges by the board of that assessment?
Cash-Flow Assumptions	<ul style="list-style-type: none">• Are they reasonable and defensible?• Are a range of scenarios considered, including a reasonable worst-case scenario?• Are they consistent with those used for the company's deferred tax and impairment assessments?

Key Areas of Accounting Risk

The EPS Initiative

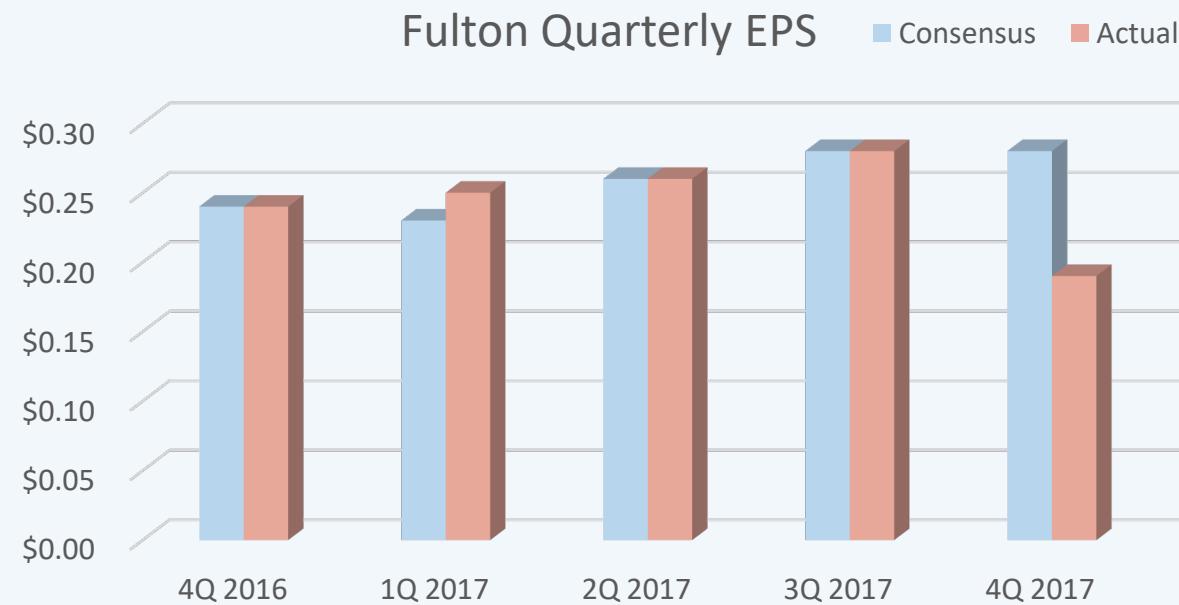
- In September 2020, the SEC announced the first of two settlements based on the Division of Enforcement's EPS (earnings per share) Initiative.
- Both settlements described issuers that met or slightly exceeded consensus EPS estimates for consecutive quarters before a significant drop in EPS.
- The Enforcement Division appears to be using the EPS Initiative to combat a practice known as "EPS smoothing" whereby issuers manage earnings to portray consistent growth rather than quarterly EPS volatility.
- The two settlements suggest that even small abnormalities can lead to enforcement investigations.

Key Areas of Accounting Risk

The EPS Initiative

FULTON FINANCIAL
CORPORATION

- *Fulton Financial Corporation*
 - During two quarters in which the company was on track to meet or beat analyst consensus EPS estimates, the company reported a valuation allowance that was at odds with the valuation methodology described in the same filing and that lowered EPS.
 - In Q2 2017, the company belatedly reversed the valuation allowance, increasing EPS by a penny in a quarter when it otherwise would have fallen short of consensus estimates.



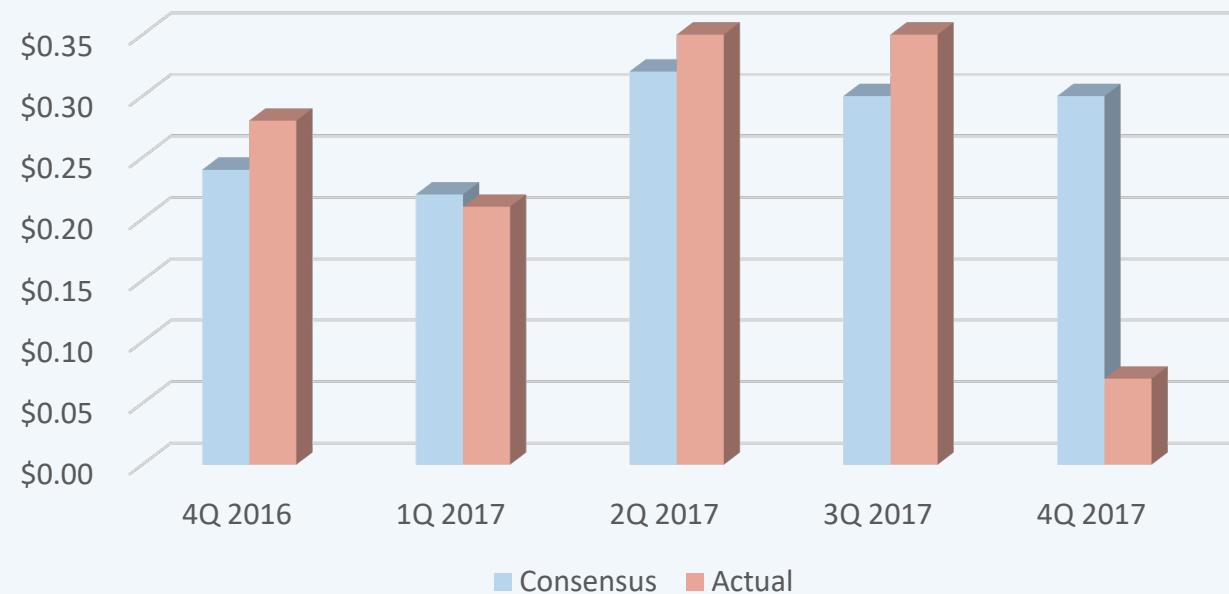
Key Areas of Accounting Risk

The EPS Initiative

Interface®

- *Interface Inc.*
 - Over several quarters in 2015 and 2016, Interface made manual accounting adjustments to bonus accruals and stock-based compensation to boost the company's income.
 - These adjustments made it possible for Interface to consistently report earnings that met or exceeded consensus estimates.

Interface Quarterly EPS



Key Areas of Accounting Risk

The EPS Initiative

- Key Takeaways
 - Repeatedly exceeding or barely meeting consensus EPS estimates is improbable over the long run and may flag the EPS Initiative's data analytics.
 - Where those streaks of meeting or exceeding consensus EPS end with a sharp decline, the probability of SEC scrutiny increases.
 - Issuers should pay particular attention to even modest adjustments to EPS that make the difference between a below-consensus EPS versus meeting or exceeding market expectations.
 - Issuers should be particularly cautious of manual adjustments to accounting estimates that require significant managerial judgment.
 - The SEC found that both companies' internal controls were insufficient to safeguard against management manipulating EPS.
 - Where manual adjustments are appropriate, issuers can better protect themselves by disclosing more details about their accounting methodology and where managerial adjustments have occurred.

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Key Areas of Disclosure Risk

Key Areas of Disclosure Risk

COVID-19 Disclosures

- On March 25, 2020, the Division of Corporation Finance released a non-exhaustive list of questions to consider when assessing the effects of COVID-19 and the disclosure obligations they may trigger.
 - How has COVID-19 impacted your financial condition and results of operations?
 - How has COVID-19 impacted your capital and financial resources, including your overall liquidity position and outlook?
 - How do you expect COVID-19 to affect assets on your balance sheet and your ability to timely account for those assets?
 - Do you anticipate any material impairments (e.g., with respect to goodwill, intangible assets, long-lived assets, right of use assets, investment securities), increases in allowances for credit losses, restructuring charges, other expenses, or changes in accounting judgments that have had or are reasonably likely to have a material impact on your financial statements?
 - Have COVID-19-related circumstances such as remote work arrangements adversely affected your ability to maintain operations, including financial reporting systems, internal control over financial reporting and disclosure controls and procedures?

Key Areas of Disclosure Risk

COVID-19 Disclosures

- Have you experienced challenges in implementing your business continuity plans or do you foresee requiring material expenditures to do so?
- Do you expect COVID-19 to materially affect the demand for your products or services?
- Do you anticipate a material adverse impact of COVID-19 on your supply chain or the methods used to distribute your products or services?
- Will your operations be materially impacted by any constraints or other impacts on your human capital resources and productivity?
- Are travel restrictions and border closures expected to have a material impact on your ability to operate and achieve your business goals?

Key Areas of Disclosure Risk

Risk Factors

- Item 105 of Regulation S-K: Companies must disclose material risk factors that *specifically* make investing in them speculative or risky as opposed to presenting risks that could apply generically to any company.
- As the impact of COVID-19 evolves over time, risk should be assessed on a continuing basis to determine if prior disclosures need revisions or supplementation.
- Pandemic-related risks may include:
 - Revenue reductions
 - Liquidity challenges
 - Market volatility for investment companies
 - Litigation risk
 - Cybersecurity risks stemming from teleworking
 - Suspension of operations due to government-mandated shutdowns
- Issuers frequently include a standalone COVID-19 risk factors section.
- Issuers should distinguish between risk factors that are purely hypothetical versus those that have already occurred.

Key Areas of Disclosure Risk

Risk Factors

- Approximately 12 private securities lawsuits have been filed alleging failure to adequately disclose risks stemming from COVID-19.
- Plaintiffs have alleged that:
 - An exchange traded fund failed to disclose the risk that crude oil prices could plummet due to reduced economic activity stemming from the pandemic and cause share prices to drop.
 - At the time of its IPO, a real estate finance company made generic disclosures regarding the risks of COVID-19 and failed to disclose specific risks about loan defaults.
 - A security software company failed to disclose the risk that conditions caused by COVID-19 could cause a merger to fall through.

Key Areas of Disclosure Risk

Management's Discussion and Analysis (MD&A)

- Item 303(a) of Regulation S-K requires issuers to discuss their “financial condition, changes in financial condition and results of operations” and to “identify any known trends or any known demands, commitments, events or uncertainties that will result in, or that are reasonably likely to result in the registrant’s liquidity increasing or decreasing in any material way.”
- MD&A should include information that, in management’s view, is necessary to understand the financial condition, changes in financial condition, and results of operations of the company.
- Issuers should consider how COVID-19 affects their MD&A disclosures.
 - Has the company needed to close any locations?
 - Has the company drawn down on bank facilities?
 - Is the company party to contracts with *force majeure* provisions that may be triggered by COVID-19?
 - Does the company need to revisit its accounting estimates?
 - What effect might the outbreak have on the company’s hedging relationships, compensation agreements, leases, and income taxes?

Key Areas of Disclosure Risk

KPIs

- The SEC has emphasized that MD&As should identify and address key performance indicators (KPIs) that assess a company's performance in relation to key business objectives.
- KPIs are often not subject to GAAP and fall outside the audited financial statements.
- In February 2020, the SEC released guidance stating that because MD&As should enable investors to see the company “through the eyes of management,” KPIs “should not deviate materially from metrics used to manage operations or make strategic decisions.”
- KPI disclosures should generally include:
 - “A clear definition of the metric and how it is calculated;
 - A statement indicating the reasons why the metric provides useful information to investors; and
 - A statement indicating how management uses the metric in managing or monitoring the performance of the business.”
 - “The company should also consider whether there are estimates or assumptions underlying the metrics or its calculation, and whether disclosure of such items is necessary for the metric not to be materially misleading.”

Key Areas of Disclosure Risk

KPIs – In The Matter of Diageo Plc

DIAGEO

- Diageo, a multinational beverage alcohol company, agreed to \$5 million to settle charges that it allegedly hit performance goals by pressuring distributors to buy products in excess of demand.
- According to the SEC, Diageo allegedly overshipped products which rendered KPIs misleading by:
 - Overstating organic growth
 - Inflating net sales and operating profit
 - Failing to describe inventory builds in excess of demand
 - Failing to describe the negative impact overshipping could reasonably be expected to have on future growth
- According to the SEC, Diageo allegedly did not have adequate disclosure procedures in place to require consideration of whether overshipping and resulting inventory builds were material trends or uncertainties that required disclosure.

Key Areas of Disclosure Risk

KPIs

- The SEC has acknowledged that issuers may need to create new KPIs or revise how they are calculated due to the effects of COVID-19.
- In January 2020, the SEC released guidance explaining that “if a company changes the method by which it calculates or presents the metric from one period to another or otherwise, the company should consider the need to disclose, to the extent material:
 - The differences in the way the metric is calculated or presented compared to prior periods,
 - The reasons for such changes,
 - The effects of any such change on the amounts or other information being disclosed and on amounts or other information previously reported, and
 - Such other differences in methodology and results that would reasonably be expected to be relevant to an understanding of the company’s performance or prospects.”

Key Areas of Disclosure Risk

Non-GAAP Financial Measures

- Continued SEC enforcement focus on use of non-GAAP. For example:
 - The SEC brought an enforcement action against ADT for presenting non-GAAP measures in the headlines and highlights of the earnings release without giving equal or greater attention to the comparable GAAP measures.
- Also, given the unusual effects of COVID-19, issuers may wish to present non-GAAP financial measures for historical periods that reflect adjustments from the required GAAP measures.

“[W]here a GAAP financial measure is not available at the time of the earnings release because the measure may be impacted by COVID-19-related adjustments,” the SEC “would not object to companies reconciling a non-GAAP financial measure to preliminary GAAP results that either include provisional amount(s) based on a reasonable estimate, or a range of reasonably estimable GAAP results.” –Division of Corporation Finance, CF Disclosure Guidance: Topic No. 9 (Mar. 25, 2020)

Key Areas of Disclosure Risk

Non-GAAP Financial Measures



"Please clarify the nature of the adjustment title 'COVID-19 shelter in place restrictions on manufacturing activities.' In your response, tell us how you reasonably quantified this adjustment, the length of time within the quarter that applied to its calculation, and the related amount applicable to the quarter ended June 30, 2020." –SEC

Comment Letter, June 22, 2020

- Microchip's response noted the following considerations with no further comment from the Staff:
 - The company calculated the equivalent number of days of lost production for each site and quantified the cost associated with their closure;
 - The charges resulted from the company's inability to operate its manufacturing activities due to restrictions imposed by the government;
 - Production had not been adversely impacted previously as a result of government restrictions and the company does not expect to incur such costs again after the pandemic has passed; and
 - The adjustment included amounts that could be objectively quantified and excluded other operational costs—e.g., increased transportation and warehousing costs, increased cleaning costs, lower production levels and inventory markdowns—that could not be clearly separated from business conditions, changes in demand, or company actions.

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Upcoming Gibson Dunn Webcasts

- December 2 | What's next? The Legislative and Policy Landscape After the 2020 Election | 12:00 – 1:00 pm EST [REGISTER](#)
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- December 10 | International Anti-Money Laundering and Sanctions Enforcement | 12:00 – 1:30 pm EST [REGISTER](#)

Publications and Recorded Webcasts

Recorded Webcasts (CLE credit available)

- [Corporate Compliance and Sentencing Guidelines](#)
- [Managing Internal Audit](#)
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- [The False Claims Act: Updates for Health Care Providers](#)
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- [The False Claims Act: Updates for the Government Contracting Sector](#)
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Publications

- Gibson Dunn COVID-19 Resources: <https://www.gibsondunn.com/category/publications/>
- Gibson Dunn White Collar Defense and Investigations: <https://www.gibsondunn.com/practice/white-collar-defense-and-investigations/>

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