

[Securities Regulation Daily Wrap Up, TOP STORY—SEC proposes to modernize Reg. S-K financial disclosures, \(Jan. 31, 2020\)](#)

Securities Regulation Daily Wrap Up

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The proposed changes are designed to enhance Management's Discussion and Analysis disclosures for the benefit of investors while simplifying compliance obligations for registrants.

The SEC has proposed amendments to its rules and forms to modernize and simplify financial disclosure requirements in Regulation S-K. The proposed amendments would eliminate duplicative disclosures and modernize and enhance Management's Discussion and Analysis disclosures to focus on material information to improve the disclosures and simplify compliance efforts. Separately, the Commission issued guidance on key performance indicators and metrics in MD&A (*Management's Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information*, [Release No. 33-10750](#), and *Commission Guidance on Management's Discussion and Analysis of Financial Condition and Results of Operations*, [Release No. 33-10751](#), January 30, 2020).

The proposal and the guidance aim to improve the quality and accessibility of the presentation of financial results and performance metrics and allow investors to make better capital allocation decisions, [said](#) Chairman Jay Clayton.

Regulation S-K changes. The proposal would eliminate Regulation S-K Items 301 and 302, and registrants would no longer be required to provide five years of selected financial data or two years of selected quarterly financial data. Item 303 (MD&A) would be amended to emphasize the principal objectives of MD&A for both full fiscal years and interim periods. In addition, registrants would disclose material cash requirements as of the latest fiscal period, the anticipated source of funds, and the general purpose of the material cash requirements. They also would disclose known events reasonably likely to cause a material change in the relationship between costs and revenues. The proposed amendments also clarify that a discussion of the reasons underlying material changes in net sales or revenues is required. Despite proposed deletions in Item 303(a), registrants would still be expected to discuss the impact of inflation or changing prices if they are part of a known trend or uncertainty that has had, or reasonably could have, a material impact on net sales or revenue or income from continuing operations.

The proposal also would replace the current more prescriptive "off-balance sheet arrangement" definition and related disclosure requirement in Item 303(a)(4) with a principles-based instruction to prompt registrants to discuss the arrangements in the broader context of MD&A. Under the new instruction, a registrant would be required to discuss commitments or obligations arising from arrangements with unconsolidated entities or persons likely to have a material effect on the registrant's financial condition. Registrants would no longer be required to provide a contractual obligations table but would explicitly be required to disclose of critical accounting estimates. The proposal also clarifies that, for material changes in a line item, disclosure of the underlying reasons for the changes in quantitative and qualitative terms is required.

The proposal also would revise the interim MD&A requirement in Item 303(b) to provide companies the flexibility to compare their most recently completed quarter to either the corresponding quarter of the prior year (as is currently required) or to the immediately preceding quarter. The Commission also proposed certain conforming amendments and parallel amendments applicable to financial disclosures provided by foreign private issuers.

Comments on the proposal are due with 60 days of publication in the *Federal Register*.

Guidance. The SEC also released guidance on key performance indicators and metrics in MD&A. The guidance states that, when registrants disclose metrics, they should consider whether additional disclosures are necessary. It also provides examples of potentially appropriate disclosures to accompany given metric, including a clear definition of the metric and how it is calculated, a statement indicating why the metric provides useful information to investors, and a discussion of how management uses the metric in monitoring business performance. The guidance also reminds companies of Exchange Act requirements to maintain disclosure controls and suggests these requirements be considered when disclosing metrics.

Commissioner statements. Commissioner Allison Herren Lee [criticized](#) the proposal for failing to address investor desire for standardized disclosure on climate change risk. "[T]he broad, principles-based 'materiality' standard has not produced sufficient disclosure to ensure that investors are getting the information they need, [and] MD&A is uniquely suited to disclosures related to climate risk," she stated. Voluntary disclosures by companies are no substitute for Commission action, she asserted and a mandatory standardized framework for climate risks would ensure comparability among companies and increase the reliability of the information disclosed.

Commissioner Hester Peirce [disagreed](#), noting that the principles-based MD&A disclosure framework provides management with flexibility to effectively tailor disclosures to provide specific information regarding a company's financial condition that is material to an investment decision. Materiality is the "longstanding touchstone" of the SEC's disclosure regime and should not be degraded by catering to the demands of select individuals or groups. "There is reason to question the materiality of ESG and sustainability disclosure based on existing practices," according to Peirce. "We ought not step outside our lane and take on the role of environmental regulator or social engineer," she said.

The releases are [No. 33-10750](#) and [No. 33-10751](#).

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