

## SEC Proposes Round Three Of Disclosure Modernization

By John O. Newell and An-Yen E. Hu

### SUMMARY

The Securities and Exchange Commission (SEC) has proposed a third group of amendments to its disclosure requirements. The proposals would generally simplify disclosure about a company's business, emphasizing a principles-based approach. The proposals would also allow the disclosure requirements in the legal proceedings section to be satisfied by links to legal proceedings disclosure included elsewhere in the report or registration statement. Finally, the proposals would change the disclosure standard for risk factors from the "most significant" to "material," require a summary of risk factor disclosures if the risk factor section is more than 15 pages, require risk factors to be organized under headings, and discourage risk factors that could apply generically to any company or any offering, but to the extent generic risk factors are presented, require companies to present them at the end of the risk factors section under a separate heading. The appendix to this alert includes the text of the proposed amendments that has been marked to show the proposed changes from current requirements.

---

The SEC continues to move forward with the updates to its disclosure requirements recommended by the SEC staff in the December 2013 [Regulation S-K study](#) prepared under a mandate in the Jumpstart Our Business Startups Act. The SEC previously adopted two rounds of amendments in [September 2018](#) (discussed in a [Goodwin alert](#)) and [April 2019](#) (discussed in another [Goodwin alert](#)). The latest proposals would revise three of the disclosure topics required by Regulation S-K in SEC reports and registration statements: Business (Item 101(a) and (c)), Legal Proceedings (Item 103) and Risk Factors (Item 105), as well as making a series of conforming changes in the text of SEC forms. The proposed amendments are subject to a 60-day public comment period after publication in the Federal Register. Companies should monitor the status of the proposed amendments.

### ***Business – Item 101(a) and (c)***

The proposed amendments to Item 101 of Regulation S-K would:

- Focus on disclosures that are material to an understanding of the company's business and replace the lengthy and detailed current list of disclosure topics with a more concise and general list of potential disclosure topics;
- Add a new disclosure topic about transactions and events that affect or may affect the company's business operations, including changes to a previously disclosed business strategy;
- Add a new disclosure topic about human capital resources, including any human capital measures or objectives that the company focuses on in managing its business, such as measures or objectives that address the attraction, development, and retention of personnel, to the extent relevant and material;

- Expand current disclosure about the impact of compliance with environmental requirements to include compliance with all material government regulations, including environmental regulations;
- Eliminate the currently required timeframe for disclosure of the general development of the company's business (generally five years, or three years for smaller reporting companies); and
- Permit a company to provide only an update of its disclosure about the general development of its business, focusing on material developments during the reporting period, in filings other than IPO registration statements. The proposed amendments would require companies that provide such an update to incorporate by reference and include an active hyperlink to the company's most recently filed disclosure that, together with the update, would present a full discussion of the general development of the company's business. A similar amendment to Item 101(h), which applies to Item 101 business disclosure by smaller reporting companies, would provide the same option for smaller reporting companies using the scaled reporting provisions.

### ***Legal Proceedings – Item 103***

The proposed amendments to Item 103 would:

- Permit companies to satisfy the disclosure requirements for material legal proceedings by providing a hyperlinked cross-reference to legal proceedings disclosure elsewhere in the report or registration statement, such as Management's Discussion and Analysis, Risk Factors or the notes to the financial statements; and
- Increase the threshold for disclosure of environmental proceedings in which a governmental authority is a party to \$300,000 from \$100,000.

### ***Risk Factors – Item 105***

The proposed amendments to Item 105 would:

- If the risk factor section is longer than 15 pages, require a risk factor summary under an appropriate heading in the forepart of the report or registration statement, consisting of a series of short, concise, bulleted or numbered statements that summarize the principal risk factors;
- Require companies to organize risk factor disclosure under relevant headings, with each risk factor under a subcaption that adequately describes the risk (as many companies currently do);
- Discourage inclusion of generic risk factors, and require companies to present any generic risk factors at the end of the risk factors section under the caption "General Risk Factors"; and
- Change the current disclosure standard from the "most significant" risk factors to "material" risk factors.

APPENDIX

**Text of Proposed Amendments to Regulation S-K Items 101, 103 and 105**  
**Additions shown in blue underscored text – ~~Deletions shown in red strikethrough text~~**

**§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

(1) In describing developments, 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) Transactions and events that affect or may affect the company's operations, including material changes to a previously disclosed business strategy;

~~(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; the nature and results of any~~

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

(iii) The nature and effects of any 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) For filings other than initial registration statements, a full discussion of the general development of the registrant's business is not required. For such filings, an update to the general development of the business disclosure with a focus on material developments in the reporting period may be provided instead of a full discussion. If a full discussion of the general development of the registrant's business is not included, pursuant to § 230.411 or § 240.12b-23 of this chapter as applicable, incorporate by reference, and include an active hyperlink to, the registrant's most recently filed disclosure that, together with the update, would present the full discussion of the general development of its business.

(23) Registrants: *[Note: the remainder of Item 101(a)(3) would remain unchanged]*

(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 material to an understanding of the registrant's business taken as a whole, the description of~~ **When describing** each ~~such~~ segment, ~~shall~~ include 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~~ **to the extent such information is material to an understanding of the business taken as a whole.**

~~(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.~~

**(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;**

**(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~~ 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.)~~

~~(iv)(ix) 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

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

(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.

~~(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]~~

~~(i)(xii) Appropriate disclosure also shall be made as to the 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~~material government regulations, including environmental regulations, may have upon the capital expenditures, earnings and competitive position of the registrant and its subsidiaries. ~~The registrant shall disclose any~~Include in such disclosure 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~~any other subsequent period that the registrant ~~may deem materials~~deems material; and~~

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

~~(ii) A description of the registrant's human capital resources, including in such description any human capital measures or objectives that management 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 attraction, development, and retention of personnel).~~

(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, except that, for filings other than initial registration statements, a smaller reporting company may provide an update to the general development of the business disclosure, instead of a full discussion, which complies with paragraph (a)(2) of this section. If the smaller reporting company has not been in business for three years, give the same information for predecessor(s) of the smaller reporting company if there are any. This business development description should include:

**§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:**

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

**(1) That involve negligence or other claims or actions if the business ordinarily results in such claims or actions, unless the claim or action departs from the normal kind of such claims or actions; or**

~~**(2) 2. No information need be given with respect to any proceeding that involves**~~ **That involve** 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) Notwithstanding paragraph (b) of this section, disclosure under this section shall include, but shall not be limited to:**

~~**(1) 3. Notwithstanding Instructions 1 and 2, any**~~ **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 administrative~~ Administrative or judicial ~~proceeding~~ 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 ~~primary~~ 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 \$~~100,000~~ 300,000; provided, however, that such proceedings which 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. ~~Do not present~~ **with relevant headings and each risk factor should be set forth under a subcaption that adequately describes the risk. The presentation of** risks that could apply generically to any registrant or any offering. ~~Explain 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) 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 forefront of the prospectus or annual report, as applicable, a series of short, concise, bulleted or numbered statements 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. 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.

**CONTACTS**

**John O. Newell**

Counsel

+1 617 570 1475

[jnewell@goodwinlaw.com](mailto:jnewell@goodwinlaw.com)

**An-Yen E. Hu**

Partner

+1 650 752 3185

[ahu@goodwinlaw.com](mailto:ahu@goodwinlaw.com)

© 2017 Goodwin Procter LLP. All rights reserved. This informational piece, which may be considered advertising under the ethical rules of certain jurisdictions, is provided with the understanding that it does not constitute the rendering of legal advice or other professional advice by Goodwin Procter LLP, Goodwin Procter (UK) LLP or their attorneys. Prior results do not guarantee similar outcome.

Goodwin Procter LLP is a limited liability partnership which operates in the United States and has a principal law office located at 100 Northern Avenue, Boston, MA 02210. Goodwin Procter (UK) LLP is a separate limited liability partnership registered in England and Wales with registered number OC362294. Its registered office is at 100 Cheapside, London EC2V 6DY. A list of the names of the members of Goodwin Procter (UK) LLP is available for inspection at the registered office. Goodwin Procter (UK) LLP is authorized and regulated by the Solicitors Regulation Authority.

IRS Circular 230 Disclosure: To ensure compliance with requirements imposed by the IRS, we inform you that any U.S. tax advice contained in this informational piece (including any attachments) is not intended or written to be used, and may not be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.