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The SEC Adopts Amendments to MD&A and Other Financial Statement Disclosures

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On November 19, 2020, the Securities and Exchange Commission (“**SEC**”) announced amendments to certain financial disclosure requirements in Regulation S-K in an effort to modernize and simplify financial disclosures. Specifically, the amendments eliminate the requirement for Selected Financial Data, streamline the requirement to disclose Supplementary Financial Information and amend disclosures required for Management’s Discussion & Analysis of Financial Condition and Results of Operations (“**MD&A**”). The full text of the final rule, which will in most cases apply to any annual report filed for the fiscal year ended December 31, 2021, may be accessed [here](#). Most notably, the amendments (i) eliminate the requirements to provide five years of select financial data under Item 301 and tabular disclosure of contractual obligations under Item 303(a)(5), (ii) limit the circumstances in which quarterly supplemental financial information must be presented under Item 302(a), (iii) clarify the objectives of MD&A and codify previous MD&A guidance and (iv) add Item 303(b)(4) to require registrants to explicitly disclose critical accounting estimates in MD&A.

The amendments were adopted in connection with the SEC’s ongoing initiative to modernize and improve disclosure by reducing costs and burdens while continuing to provide investors with all material information.

Amendments

The following table, which is not intended to be comprehensive, summarizes the amendments to Items 301, 302(a), 303(a) and 303(b) of Regulation S-K:

RULE	AMENDMENTS SUMMARY
<p>Selected Financial Information</p> <p>Reg. S-K Item 301 (eliminated)</p>	<p>As currently in effect, Item 301 of Regulation S-K (subject to certain exceptions for Smaller Reporting Companies (“SRCs”) and Emerging Growth Companies) requires a registrant to furnish selected financial data in comparative tabular form for each of the registrant’s last five fiscal years and any additional years necessary to keeping the information from being misleading. The original purpose of the rule was to elicit disclosure of material trends. Under the final rule, Item 301 will be eliminated; however, the SEC noted that registrants are encouraged to consider whether trend information for periods earlier than those presented in the financial statements may be necessary to provide material information relevant to an assessment of a registrant’s financial condition and results of operations.</p>

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<p>Supplementary Financial Information</p> <p>Reg. S-K Item 302(a)</p>	<p>Once the new Item 302(a) is effective, registrants will no longer be required to provide two years of tabular selected quarterly financial data. The requirements under the current Item 302(a) will be replaced with a “principles-based requirement for material retrospective changes.”</p> <p>Currently, Item 302(a) of Regulation S-K requires disclosure of, among other things, (i) selected quarterly financial data of specified operating results, (ii) variances in these results from amounts previously reported on a Form 10-Q and (iii) a description of the effect of any discontinued operations and unusual or infrequently occurring items recognized in each quarter, as well as the aggregate effect and the nature of year-end or other adjustments that are material to the results of that quarter.</p> <p>Although Item 302(a) will be retained, disclosure will be required only when there are one or more retrospective changes that, in the aggregate, are material to the statements of comprehensive income for any of the quarters within the registrant’s two most recent fiscal years and any subsequent interim period for which financial statements are included or required to be included by Article 3 of Regulation S-X. The amendments will require registrants to provide an explanation of the reasons for such material changes and to disclose, for each affected quarterly period and the fourth quarter in the affected year, summarized financial information related to the statements of comprehensive income and earnings per share reflecting such changes. Depending on the circumstances, the affected quarters may include a single quarter or may flow through to several quarters within the two-year look-back period.</p> <p>The new rule also amends the definition of “summarized financial information” to allow for variations in disclosures to conform to the nature of a registrant’s business and allow registrants flexibility in the line items presented.</p> <p>Examples of such retrospective changes that may require disclosure if material include (i) reorganization of entities under common control, (ii), a disposition of a business that is accounted for as discontinued operations, (iii) correction of an error and (iv) certain changes in accounting principles.</p> <p>In streamlining the requirements of Item 302(a), the SEC stated that the amendments will eliminate duplicative disclosures that are “provided elsewhere, such as in Forms 10-Q or, in the case of fourth quarter results, can be derived from annual results disclosed in the Form 10-K.”</p>

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<p>Summary of Reg. S-K Item 303</p>	<p>The SEC final rule amends multiple portions of the disclosures required in MD&A. As currently in effect, Item 303 of Regulation S-K requires disclosure of information relevant to assessing a registrant’s financial condition, changes in financial condition and results of operations. More specifically, Item 303(a) requires disclosure of five key components: liquidity, capital resources, results of operations, off-balance sheet arrangements and contractual obligations. Item 303(b) covers interim period disclosures and requires registrants to discuss material changes in the items listed in Item 303(a), other than the impact of inflation and changing prices on operations. Item 303(c) acknowledges the application of a statutory safe harbor for forward-looking information provided in off-balance sheet arrangements and contractual obligations disclosures, and Item 303(d) provides certain accommodations for SRCs.</p>
<p>Purpose of MD&A Reg. S-K Item 303(a)</p>	<p>As amended, the new Item 303(a) emphasizes the principal objectives of MD&A and specifies information that registrants must disclose in order to allow investors to “view the registrant from management’s perspective.” Registrants must disclose “matters that are reasonably likely, based on ‘management’s assessment,’ to have a material impact on future operations,” including the following:</p> <ul style="list-style-type: none"> • Material information relevant to an assessment of the financial condition and results of operations of the registrant, including an evaluation of the amounts and certainty of cash flows from operations and from outside sources. • Material events and uncertainties known to management that are reasonably likely to cause reported financial information not to be indicative of future operating results or of future financial condition. This includes descriptions and amounts of matters that have had a material impact on reported operations as well as matters that are reasonably likely, based on management’s assessment, to have a material impact on future operations. • The material financial and statistical data that the registrant believes will enhance a reader’s understanding of the registrant’s financial condition, cash flows and other changes in financial condition, and results of operations.
<p>Key MD&A Changes Reg. S-K Item 303(b)</p>	<p>Under the amendments, current Item 303(a) will be re-captioned as Item 303(b) and will update the required disclosures concerning capital resources, results of operations, off-balance sheet arrangements and contractual obligations. In addition, the text of the new Item 303(b) will require a discussion of “the underlying</p>

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	<p>reasons for” material changes in qualitative and quantitative terms, rather than simply the “causes” for material changes. Instead of simply reciting which numbers have changed, registrants should instead explain why those changes occurred in both qualitative and quantitative terms. When the reasons for material changes are interrelated, registrants should acknowledge this, and should explain the interrelation of reasons to the extent possible.</p> <p>A summary of key changes to the new Item 303(b) is provided below:</p> <ul style="list-style-type: none"> • <u>Capital Resources</u>. Currently, registrants are required to discuss their material commitments for capital expenditures, and to indicate the general purpose of and the anticipated sources of funds needed to fulfill such commitments. The new rule expands this disclosure by requiring that registrants broadly disclose material cash commitments, including but not limited to capital expenditures. Specifically, a registrant must describe their material cash “requirements,” including commitments for capital expenditures, the anticipated source of funds needed to satisfy such cash requirements, and the general purpose of such requirements. The “requirements” category is intended to encompass a broader range of significant cash commitments, such as intellectual property and human capital, which for some registrants may be as significant or more so than capital expenditures, which are a registrant’s expenditures on its physical assets. • <u>Known Trends or Uncertainties</u>. Currently, registrants must describe any known trends or uncertainties that have had or that the registrant reasonably expects will have a material impact (favorable or unfavorable) on net sales or revenues or income from continuing operations. The amendments provide that a registrant must now disclose known events that are “reasonably likely” to cause a material change, as opposed to those events that “will” have a material impact. This lowers the threshold for disclosure, as the SEC has specified that events are “reasonably likely” to cause a material change if the reasonable investor would consider the omission of such events as significantly altering the mix of information provided in a registrant’s disclosures. Determining whether to disclose information under this standard will require balancing the likelihood that an event will occur and the materiality of such event occurring. • <u>Net Sales and Revenues</u>. Currently, Item 303(a)(3)(iii) specifies that, to the extent the financial statements disclose “material

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	<p>increases” in net sales or revenues, a registrant must provide a narrative discussion of the extent to which such “increases” are attributable to increases in prices, or to increases in the volume or amount of goods or services being sold, or to the introduction of new products or services. As many registrants already do, the final rule will require disclosures of “material changes”, not only increases in net sales or revenues.</p> <ul style="list-style-type: none"> <li data-bbox="467 638 1273 909">• <u>Inflation and Price Changes.</u> Registrants are no longer required to specifically reference the impact of inflation and price changes on a registrant’s net sales, revenue and income from continuing operations, to the extent material. However, if material, registrants are still required discuss the impact of inflation or price changes if they are part of a known trend or uncertainty that has had, or is reasonably likely to have, a material favorable or unfavorable impact on net sales, revenue, or income from continuing operations. <li data-bbox="467 947 1273 1276">• <u>Off-Balance Sheet Arrangements.</u> The current requirement will be replaced with a new principles-based instruction requiring registrants to discuss commitments or obligations, including contingent obligations, arising from arrangements with unconsolidated entities or persons that have, or are reasonably likely to have, a material current or future effect on a registrant’s financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, cash requirements, or capital resources. Rather than requiring a separately-captioned section, this disclosure is expected to be incorporated into the broader MD&A discussion of liquidity and capital resources. <li data-bbox="467 1314 1273 1585">• <u>Critical Accounting Estimates.</u> In accordance with prior SEC guidance, the final rule adds the new Item 303(b)(4), which explicitly requires disclosure of critical accounting estimates. For each critical accounting estimate, registrants must disclose why the estimate is subject to uncertainty, and, to the extent material and reasonably available, how much each estimate has changed during the relevant period, and the sensitivity of the reported amounts to the methods, assumptions, and estimates underlying the estimate’s calculation. <li data-bbox="467 1623 1273 1772">• <u>Segment Reporting.</u> The new Item 303(b) will require registrants to discuss each relevant “product line” to the extent this is necessary to understand the registrant’s business, in addition to the current requirements to discuss each segment and subdivision (e.g. geographic area) to the extent relevant. <li data-bbox="467 1810 1273 1839">• <u>Elimination of Contractual Obligations Table.</u> The new Item

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	303(b) eliminates the requirement under the current Item 303(a)(5) to provide a contractual obligations table in tabular format. Registrants must, however, discuss material cash requirements, including material contractual obligations, in their liquidity and capital resources discussion.
Interim Period Adjustments Reg. S-K Item 303(c)	The new Item 303(c) (currently Item 303(b)) permits registrants to compare their most recently completed quarter to either the corresponding quarter of the prior year (as is currently required) or the immediately preceding quarter. The SEC expects that this amendment will provide flexibility and “a more tailored and meaningful analysis” concerning a registrant’s business cycles.

Applicability

The final rule will apply to foreign private issuers providing disclosure required by Form 20-F or Form 40-F. In addition, for those disclosure requirements applicable to SRCs, such as the discussion of liquidity and capital resources, Item 303(d) has been amended to mirror the disclosure requirements of non-SRC registrants.

Effective Dates of Amendments

The amendments will become effective February 10, 2021, and registrants will be required to comply with the amended rules for their first fiscal year ending on or after August 9, 2021. For most registrants (calendar-year companies), this means that they must comply with the amendments for their Annual Report on Form 10-K filed for the year ended December 31, 2021. However, registrants may voluntarily comply with any amended item at any time after the amendments become effective, provided that they comply with such amended item in its entirety and continue to comply with such amended item in any applicable filings going forward.

For additional information, please contact any member of Haynes and Boone’s [Capital Markets and Securities Practice Group](#).