January 16, 2024

Preparing for the 2024 Annual Report and Proxy Statement Season

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This alert highlights recent updates to Securities and Exchange Commission ("SEC") disclosure obligations effective for the 2024 Form 10-K and proxy statement season as well as other regulatory updates companies should consider. Note that the topics listed below include key SEC and stock exchange required updates and do not cover other updates that companies should take into consideration, such as voting guidelines of proxy advisory firms and institutional investors, which are beyond the scope of this alert.

Cybersecurity

The SEC has adopted disclosure rules addressing cybersecurity incidents as well as cybersecurity risk management, strategy, and governance, which included amendments to (i) Form 8-K through the addition of Item 1.05, (ii) Form 10-K through the addition of Item 106 to Regulation S-K, and (iii) Forms 6-K and 20-F, providing for generally parallel disclosure requirements for foreign private issuers ("FPIs"). Current report disclosures (Form 8-K and Form 6-K) were required beginning on December 18, 2023, and smaller reporting companies ("SRCs") are not required to comply with the current report requirement until June 15, 2024. All companies (including SRCs and FPIs) are required to include the periodic report disclosures, beginning with annual reports for fiscal years ending on or after December 15, 2023.

Form 8-K Disclosure

New Item 1.05 to Form 8-K requires companies to describe, to the extent known at the time of filing, the material aspects of the nature, scope, and timing of a cybersecurity incident, and the material impact or reasonably likely material impact on the company, including on its financial condition and results of operations. Companies must also disclose whether information required by Item 1.05 has not been determined or is unavailable at the time of filing. If such information is not initially available, companies must subsequently file an amendment to the Form 8-K within four business days after determining such information or it becomes available. Due to substantial risks to national security or public safety, the SEC has allowed for filing delays (up to 30, 60 or 120 business days or more, subject to SEC approval) if the U.S. Attorney General (the "AG") determines, and notifies the SEC in writing, that disclosure of a cybersecurity incident would pose such risks.

The SEC and several governmental agencies have recently provided additional guidance with respect to the implementation of Item 1.05 to Form 8-K. The SEC's Division of Corporation Finance (the "Staff") recently released new compliance and disclosure interpretations ("C&DIs") regarding material cybersecurity incidents and Form 8-K filing delays, which are available here. Furthermore, on December 6, 2023, the Federal Bureau of Investigation (the "FBI") published a Policy Notice to establish procedures by which the FBI will document cybersecurity incident delay requests. The full text of the FBI's Policy Notice is available here. Additionally, on December 12, 2023, the Department of Justice ("DOJ") outlined the process for companies to request that the AG authorize delays of cybersecurity incidents that would otherwise be required to be disclosed under Item 1.05 of Form 8-K. The full text of the DOJ guidelines are available here.

Form 10-K Disclosure

New Item 1C of Form 10-K requires domestic filers to provide a description of their processes, if any, for assessing, identifying, and managing material risks from cybersecurity threats in sufficient detail for a reasonable investor to understand those processes. Additionally, companies must provide a description of whether any risks from cybersecurity threats, including those resulting from previous cybersecurity incidents, have materially affected or are reasonably likely to materially affect the company, including its impact on business strategy, results of operations, or financial condition. FPIs have generally parallel disclosure requirements with respect to the Form 20-F.

The rules also require descriptions of the roles of the board of directors and management in overseeing and implementing cybersecurity processes and assessing and managing cybersecurity-related risks. A company must identify any board committee or subcommittee responsible for oversight and describe the processes by which the board or such committee is informed of such risks. Item 106(c)(2) provides a non-exhaustive list of elements to consider when disclosing management's role in assessing and managing the company's material risks from cybersecurity threats.

For more information on the new cybersecurity rules, please see this Haynes and Boone alert.

Rule 10b5-1 Insider Trading Plans and Related Disclosures

The SEC introduced new amendments and disclosure requirements under Rule 10b5-1 of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), in an effort to expand investor protections concerning insider trading.

Amendments to Affirmative Defense to Insider Trading Liability

The SEC amended the Rule 10b5-1(c)(1) affirmative defense to insider trading liability, and such final rules became effective on February 27, 2023. Among other things, the final rules (i) impose a cooling-off period before trades may occur under a plan covering officers and directors of the later of (1) 90 days following plan adoption or modification or (2) two business days following the disclosure in periodic reports on Forms 10-Q or 10-K of the issuer's financial results for the fiscal quarter in which the plan was adopted or modified (with a maximum cooling off period of 120 days after the adoption or modification of a plan), (ii) impose a cooling-off period before trades may occur under a plan for persons other than officers and directors of 30 days from adoption or modification of a plan, (iii) require directors and officers to include a representation in their plan certifying, at the time of the adoption, that (1) they are not aware of material nonpublic information about the issuer or its securities and (2) they are adopting the plan in good faith and not as part of a plan or scheme to evade the prohibitions of Rule 10b-5, (iv) require all persons entering into a Rule 10b5-1 plan to act in good faith with respect to that plan in order to rely on the Rule 10b5-1(c)(1) affirmative defense, (v) limit the ability of anyone other than issuers to use multiple overlapping Rule 10b5-1 plans and (vi) provide that a person other than the issuer may rely on the Rule 10b5-1(c)(1) affirmative defense for only one single-trade plan during any 12-month period.

Disclosure Requirements

New Item 408(a) requires companies to disclose on Forms 10-Q and 10-K whether any Section 16 officer or director adopted, modified, or terminated a Rule 10b5-1 plan or a "non-Rule 10b5-1 trading arrangement" during the prior quarter. For all companies except SRCs, the requirement became effective with the filing covering the first full fiscal quarter that began on or after April 1, 2023. SRCs must comply with the requirement beginning with the filing covering

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the first full fiscal quarter beginning on or after October 1, 2023, which for calendar year-end SRCs is the Form 10-K for the fiscal year ended 2023.

For each trading arrangement that is adopted, modified, or terminated, the disclosure must identify whether the trading arrangement is a Rule 10b5-1 plan or a non-Rule 10b5-1 trading arrangement, and provide a brief description of the material terms (other than price), including (i) the name and title of the director or officer; (ii) the date of adoption, modification, or termination of the trading arrangement; (iii) the duration of the trading arrangement; and (iv) the aggregate number of securities to be sold or purchased under the trading arrangement (including pursuant to the exercise of any options).

Companies should be aware that additional disclosures related to insider trading policies and option grants will be required in the Form 10-K for the fiscal year ending December 31, 2024 and the proxy statement for the 2025 annual meeting. New Item 408(b) will require issuers to provide annual disclosure of insider trading policies and procedures in Form 10-K and proxy and information statements, and new item 601(b)(19) will require issuers to file their insider trading policies and arrangements with their Form 10-K. Under new Item 402(x), issuers will be required to disclose in Form 10-K or proxy and information statements information regarding awards of options close in time to the release of material nonpublic information. Issuers will also be required to disclose, in tabular format, any awards granted during the last completed fiscal year to named executive officers ("NEOs") that were granted within four business days before or one business day after filing a periodic report on Form 10-Q or Form 10-K, or filing or furnishing of a current report on Form 8-K that discloses material nonpublic information.

For more information on the new Rule 10b5-1 insider trading plans and related disclosures, please see this Haynes and Boone alert.

Clawback Rules Under Dodd-Frank

The SEC implemented the incentive-based compensation recovery provisions of the Dodd-Frank Act, which directed the national stock exchanges to establish clawback listing standards. The NYSE and Nasdaq's respective clawback listing standards required that listed companies adopt compliant clawback policies by December 1, 2023.

In addition to adopting clawback policies, companies must (i) file their written clawback policies as exhibits to their annual reports, (ii) indicate by checkboxes on the cover pages of their annual reports whether the financial statements included in the filings reflect a correction of an error to previously issued financial statements and whether any of those corrections are restatements requiring a recovery analysis of incentive-based compensation under their clawback policies, and (iii) disclose how they have applied their clawback policies during or after the last completed year.

For more information on the clawback rules, please see this Haynes and Boone alert.

Update to Sub-Certifications

With respect to the new rules regarding cybersecurity disclosures, Rule 10b5-1 insider trading plans and related disclosures and restatements and related clawbacks, companies should update as necessary their sub-certifications completed by employees to support the Form 10-K certifications executed by the company's CEO and CFO.

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Share Repurchase Disclosure Modernization

In May 2023, the SEC adopted amendments requiring disclosures related to issuers' share repurchase activity, which would require issuers to (i) disclose daily repurchase activity quarterly or semiannually depending on the issuer, (ii) include a checkbox indicating if certain directors or officers traded in the relevant securities within four business days before or after the public announcement of an issuer's repurchase plan or program, (iii) provide narrative disclosure about the issuer's repurchase practices in its periodic reports, and (iv) provide quarterly disclosure in an issuer's periodic reports on Form 10-K and Form 10-Q related to an issuer's adoption and termination of 10b5-1 trading plans.

Following litigation in the U.S. Court of Appeals for the Fifth Circuit (the "Fifth Circuit"), the Fifth Circuit held that the SEC acted arbitrarily and capriciously in adopting the rule, in violation of the Administrative Procedures Act, when it failed to respond to comments on the rule and conduct a proper cost-benefit analysis. Therefore, the Fifth Circuit directed the SEC to correct the rule's defects within 30 days. The SEC filed a letter stating that it would not be able to correct the defects within the allotted time after the Fifth Circuit denied the SEC's prior motion for additional time to correct the defects. As a result, the Fifth Circuit vacated the rule on December 19, 2023. It is possible that the SEC will appeal the Fifth Circuit's ruling or take some other regulatory action; however, this decision means that public companies are not required to comply with the updated repurchase disclosure rules at this time.

For more information on the Fifth Circuit's decision, please see this Haynes and Boone alert.

Amendments to Section 13 Beneficial Ownership Reporting Requirements

The SEC adopted amendments to the requirements for beneficial ownership reporting on Schedules 13D and 13G under Section 13 of Exchange Act. Most notably, these amendments accelerate filing deadlines for Schedules 13D and 13G. Initial filings on Schedule 13D will be due within five business days (instead of 10 business days) of acquiring more than 5% of beneficial ownership or losing eligibility to file on Schedule 13G, and amendments due to a material change in ownership must be filed within two business days (instead of "promptly").

The new rules also accelerate the initial filing and amendment deadlines for Schedule 13Gs as follows:

- Qualified Institutional Investors:
  - Initial Filings due within 45 days after calendar quarter-end (instead of 45 days after calendar year-end) in which beneficial ownership exceeds 5%, and 5 business days (instead of 10 calendar days) after month end in which beneficial ownership exceeds 10%.
  - Amendments for any material change (instead of any change) due 45 days after calendar quarter-end (instead of 45 days after calendar year-end), and 5 business days (instead of 10 calendar days) after month-end if surpassing 10%, and thereafter, 5 business days (instead of 10 calendar days) after month-end for a 5% or more change in ownership.
- Exempt Investors:
  - Initial filings due within 45 days after calendar quarter-end (instead of 45 days after calendar year-end) in which beneficial ownership exceeds 5%.

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  - Amendments for any material change (instead of any change) due 45 days after calendar quarter-end (instead of 45 days after calendar year-end).

- Passive Investors:

  - Initial filings due within 5 business days (instead of 10 calendar days) after acquiring beneficial ownership of more than 5%.

  - Amendments for any material change (instead of any change) due 45 days after calendar quarter-end (instead of 45 days after calendar year-end) and 2 business days (instead of promptly) after surpassing 10%, and thereafter, 2 business days (instead of promptly) after 5% or more change in ownership.

The SEC clarified in the adopting release that the rules governing amended Schedules 13D and 13G will now share the same materiality standard for determining when an amendment is triggered. As a result, the Schedule 13D amendment trigger relating to any acquisitions or dispositions of 1% or more of the outstanding class of securities is equally instructive for Schedule 13G purposes.

As a result of the accelerated filing deadlines, the amendments extend the cutoff time for filing Schedules 13D and 13G on EDGAR to 10:00 p.m. Eastern Time.

Additionally, the new rules provide guidance on when holders of certain derivative securities are deemed to beneficially own the referenced security, as well as guidance on when a “group” is formed for purposes of beneficial ownership reporting. The SEC stated that group formation does not require an express agreement and “depending on the facts and circumstances, concerted actions by two or more persons for the purpose of acquiring, holding or disposing of securities of an issuer are sufficient to constitute the formation of a group.” The amendments also require reporting of cash-settled derivative securities under Item 6 of Schedule 13D regardless of whether such derivative security was originated, offered or sold by the issuer. Compliance with the revised Schedule 13D deadlines and all other amendments will be required on February 5, 2024, and compliance with the revised Schedule 13G deadlines will be required beginning September 30, 2024.

In addition to the accelerated filing deadlines, the amendments require filers to file Schedules 13D and 13G in a structured, machine-readable format beginning December 18, 2024, although filers may continue to file exhibits in an unstructured data format.

For more information on the amendments to Section 13 beneficial ownership reporting requirements, please see this Haynes and Boone alert.

“Without Merit” in Litigation Disclosure

Companies should carefully review their litigation disclosures in light of a recent court decision. In *City of Fort Lauderdale Police Firefighters’ Retirement System v. Pegasystems, Inc.* (“Pegasystems”), Pegasystems maintained that litigation claims were “without merit” in multiple SEC filings, including its Form 10-K filed on February 16, 2022. However, in May of 2022, such litigation resulted in a more than $2 billion judgment against Pegasystems, and the Pegasystems share price dropped 28 percent in the next two days.

The court found that Pegasystems misled investors when Pegasystems reassured investors in its Form 10-K and other statements that existing claims were “without merit” because investors may draw improper conclusions when

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a company makes “misleading substantive declarations regarding its beliefs about the merits of the…litigation.” If reasonably believed to be true, a company may include the following type of disclosure as opposed to asserting that litigation against a company is “without merit”:

- “We plan to vigorously defend ourselves.”
- “We believe we have substantial defenses.”
- “We intend to pursue all available administrative and judicial remedies necessary to resolve these matters.”
- “We intend to dispute these allegations.”

Pay Versus Performance: Recommendations for 2024 Disclosures

The SEC released C&DIs and issued numerous comment letters in 2023 on registrant “pay-versus-performance” disclosures required pursuant to Item 402(v) of Regulation S-K. Highlights include:

- Companies should use only one company selected measure (“CSM”) in their pay versus performance (“PVP”) Table, unless doing so would be misleading. (C&DI 128D.09 and recent comment letters) Additionally, companies cannot use a CSM that is measured over a multi-year period. The measurement should only be for the most recent fiscal year. (C&DI 128D.11)
- If retirement eligibility is the sole vesting condition for a stock or option award, this condition would be considered satisfied for the purposes of Item 402(v) of Regulation S-K disclosure and should be included in the calculation of executive compensation actually paid in the year that the holder becomes retirement eligible. (C&DI 128D.18)
- If a company loses SRC status during a fiscal year, the company may continue to provide scaled PVP disclosure in its definitive proxy or information statement filed not later than 120 days after that fiscal year. (C&DI 128D.28) However, if a company was an emerging growth company (“EGC”) and loses its EGC status, the company must provide the required PVP disclosure in any proxy statement or information statement filed after it loses EGC status. (C&DI 128D.29)
- In calculating equity awards for NEOs, companies should include any change in value of equity awards during the time as NEO when calculating the total compensation actually paid. (C&DI 128D.02)
- The calculation of executive compensation actually paid should include dividends or dividend equivalents paid that are not already reflected in the fair value of stock awards or included in another component of total compensation. (C&DI 128D.23)
- If a registrant has multiple principal executive officers in a given fiscal year, the registrant may aggregate the compensation for a given year, so long as it is not misleading. (C&DI 128D.13) Each NEO must be included individually in the calculation of average compensation amounts. In such cases, the registrant should consider including additional disclosure on the impact of the inclusion of such individuals on the calculation in order to provide clarity to investors. (CD&I 128D.30)

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- If using a peer group from the company's Compensation Discussion and Analysis ("CD&A") section, make sure that for each year in the PVP Table, the peer group of that year's CD&A is used and disclose changes to membership of the peer group year to year. (C&DI 128D.07 and recent comment letters)

- Companies should disclose the relationships between compensation and: (1) total shareholder return ("TSR"), (2) net income, and (3) the CSM. The SEC will not accept a statement that "no relationship exists." (Recent comment letters)

- Companies should clarify what peer group is used to determine peer group TSR and describe the relationship between company TSR and peer group TSR. (Recent comment letters)

- When identifying a TSR peer group, companies should include a footnote disclosing the index chosen. If the registrant chooses to use a different published industry or line-of-business index from that used by it for the immediately preceding fiscal year, explain by footnote the reason(s) for this change and compare the registrant's cumulative total return with that of both the newly selected peer group and the peer group used in the immediately preceding fiscal year. (CD&I 128D.24)

- Comparison of the registrant's cumulative total return with that of both the newly selected peer group and the peer group used in the immediately preceding fiscal year is not required if (1) an entity is omitted solely because it is no longer in the line of business or industry, or (2) the changes in the composition of the index/peer group are the result of the application of pre-established objective criteria. In these two cases, describe the change and the basis for the change, including the names of the companies deleted from the new index/peer group. (CD&I 128D.27)

- Item 402(v)(2)(iv) does not contemplate the use of a broad-based equity index as a peer group for purposes of the PVP disclosure. (CD&I 128D.25)

- For purposes of Item 402(v)(2)(iv), the weighting requirement is applicable only if the registrant is not using a published industry or line-of-business index. (CD&I 128D.26)

- Any reference to "Net Income" or "Net Loss" in the PVP table should refer only to "Net Income" or "Net Loss" as proscribed by GAAP. (Recent comment letters)

- Companies must disclose how any non-GAAP measure is calculated from the audited financial statements. Registrants can cross reference in the same document, but incorporation by reference to another document is not permitted. Additionally, supplemental disclosures must not be misleading, may not be presented with greater prominence than required disclosures, and must include a clear description of the relationship to compensation actually paid for each supplemental measure, across all fiscal years presented. (Recent comment letters)

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Non-GAAP Compliance and Disclosure Interpretations Updates

The SEC updated its non-GAAP C&DIs in December 2022 to expand its guidance on usage of non-GAAP numbers that the SEC might consider "misleading" under Item 10(e) of Regulation S K and Regulation G.

C&DI 100.01 clarifies that presenting a non-GAAP performance measure that excludes normal, recurring, cash operating expenses necessary to operate the business could be misleading, explaining that it considers operating expenses that occur "repeatedly or occasionally including at irregular intervals" as recurring.

C&DI 100.04 explains that non-GAAP measurements could be considered misleading under Regulation G if the recognition and measurement principles used to calculate the measures are inconsistent with GAAP, such as changing the way the company recognizes income, presenting a measure of revenue as gross when GAAP requires net, or vice versa, or changing accounting of revenue and expenses from accrual to cash.

C&DI 100.05 states that a non-GAAP measure may be misleading if it, and/or any adjustment made to the GAAP measure, is not appropriately labeled and clearly described and provides examples of inappropriate labeling and descriptions that would cause a measure to violate Rule 100(b) of Regulation G.

C&DI 100.06 articulates the Staff's view that a non-GAAP measure can be misleading and violate Rule 100(b) of Regulation G, even if accompanied by disclosure about the nature and effect of each adjustment made to the most directly comparable GAAP measure. However, the Staff did not provide examples to clarify.

C&DI 102.10 provides new and updated examples of instances where the presentation of a non-GAAP measure are more prominent than the comparable GAAP measures, thus violating Regulation G and Item 10(e) Regulation S-K:

- Presenting an income statement comprised of non-GAAP measures with all or most of the line items and subtotals that would be found in a GAAP income statement;
- Presenting a non-GAAP measure before the most directly comparable GAAP measure or omitting the GAAP measure entirely;
- Presenting a non-GAAP measure in an earnings release headline or caption before or without the most directly comparable GAAP measure;
- Presenting a forward-looking non-GAAP measure in reliance on the exception under Item 10(e)(1)(i)(B) of Regulation S-K without disclosing reliance upon the exception, without identifying the information that is unavailable and without placing the information's probable significance in a location of equal or greater prominence;
- Presenting a ratio with a non-GAAP measure as a numerator or denominator without presenting a ratio using the most directly comparable GAAP measure with equal or greater prominence;
- Reconciling a non-GAAP measure to another non-GAAP measure and not a GAAP measure; and
- Presenting tabular disclosure of non-GAAP disclosure through charts, tables, or graphs without presenting charts, tables, or graphs of the comparable GAAP measures with equal or greater prominence.

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Corporate Transparency Act

Effective January 1, 2024, the beneficial ownership reporting requirements set forth in the Corporate Transparency Act (the "CTA") and the related regulations adopted by the U.S. Treasury's Financial Crimes Enforcement Network ("FinCEN") require each "reporting company" formed during 2024 to file an initial report with identifying information about itself and its beneficial owners as well as company applicants within 90 days from the date of formation. Reporting companies formed before January 1, 2024 will have until January 1, 2025 to file their initial reports, and reporting companies formed during and after 2025 will have 30 days post-formation to file. Once the initial report has been filed, both existing and new reporting companies must update their reports within 30 days of a change.

Under the CTA, "reporting companies" include all domestic non-exempt corporations, limited liability companies, limited partnerships, and other entities created by filing a document with a secretary of state or similar office. Foreign entities registered to do business in the United States are also reporting companies under the final regulations. However, exemptions are available for certain businesses that are already heavily regulated or otherwise subject to significant reporting requirements, such as banks, publicly traded companies, broker-dealers, and public accounting firms. In addition, "large operating companies" that have an operating presence at a physical office in the United States, $5 million in gross receipts or sales from U.S. sources on their previous year's federal tax return, and over 20 full-time employees are exempt from these reporting requirements. Controlled or wholly owned subsidiaries of certain exempt entities, including wholly-owned subsidiaries of public companies, are exempt under the CTA.

For an overview of the CTA, please see this Haynes and Boone alert covering the beneficial ownership regulations as well as this Haynes and Boone alert covering FinCEN's access rules.

For further information, please contact a member of the Haynes and Boone Capital Markets and Securities Practice Group.

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