



Securities Quarterly Update

January 2021 | Winter Edition

Welcome to the winter edition of Securities Quarterly Update, a publication that provides updates and guidance on securities regulatory and compliance issues. In this edition, we look at ongoing disclosure developments, including those related to COVID-19, that public companies should consider as they prepare their Form 10-K filings for the fiscal year ended December 31, 2020, as well as other general updates in securities laws and regulations.

SEC Rule Amendments to MD&A and Financial Disclosures Under Regulation S-K

On November 19, 2020, the [SEC announced its adoption of a Final Rule to amend, simplify and enhance certain financial disclosure requirements under Regulation S-K](#). The amendments eliminate the requirement to provide selected financial data (Item 301), replace the requirement for tabular supplementary financial information (Item 302) with a principles-based disclosure requirement regarding material retrospective changes, and make significant changes to Management's Discussion and Analysis (MD&A) (Item 303). The SEC also adopted conforming amendments to its forms. The amendments' impacts on the [Final Rule](#) are summarized below. As is currently the case, smaller reporting companies are not required to provide disclosures under Items 301 and 302.

Selected Financial Data (Item 301)

Item 301 (Selected Financial Data), which had required companies to provide five-year comparative tabular financial data, was eliminated. Nevertheless, the SEC encourages companies to consider whether trend information for periods earlier than those presented in the financial statements should be included as part of MD&A's objective to "provide material information relevant to an assessment of the financial condition and results of operations" and whether a tabular presentation of relevant

financial or other information in an introductory section may improve a reader's understanding of MD&A.

Supplementary Financial Information (302(a))

The amendments to Item 302(a) replace the current requirement for two-year quarterly tabular disclosure with a principles-based requirement for disclosure regarding material retrospective changes, such as changes in accounting principles, reorganizations, discontinued operations or corrections of errors.

Current Item 302(a)(1) requires disclosure of selected quarterly financial data of specified operating results and current Item 302(a)(2) requires disclosure of variances in these results from amounts previously reported on a Form 10-Q. The SEC's amendments clarify that the disclosure of summary financial information may vary, as appropriate, to conform to the nature of the company's business and aim to eliminate duplicative disclosures.

The Final Rule retains Item 302(a), "streamlining its requirements to require disclosure only when there are one or more retrospective changes that pertain to the statements of comprehensive income for any of the quarters within the 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 and that, individually or in the aggregate, are material." The amendments require companies "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 (as specified in Rule 1-02(bb)(ii) of Regulation S-X) and earnings per share reflecting such changes.”

MD&A (Item 303)

Item 303 of Regulation S-K requires disclosure of information relevant to assessing a company’s financial condition, changes in financial condition and results of operations. The amendments to Item 303 emphasize the importance of materiality and trend disclosures, better enabling investors to view the company through the same lens as management, outline the tests for trend disclosures, and include the following changes:

- (1) **Revision to Item 303(a)(3)(ii) (Capital Resources)**, now requiring companies to describe “material cash requirements, including commitments for capital expenditures, as of the latest fiscal period, the anticipated source of funds needed to satisfy such cash requirements, and the general purpose of such requirements.”
- (2) **Revision to Item 303(a)(3)(ii) (Results of Operations)**, now requiring companies “to disclose known events that are reasonably likely to cause a material change in the relationship between costs and revenues, such as known or reasonably likely future increases in costs of labor or materials or price increases or inventory adjustment.”
- (3) **Revision to Item 303(a)(3)(iii) (Results of Operations)**, clarifying that “a discussion of material changes in net sales or revenue is required (rather than only material increases)” (which represents codification of the SEC’s existing interpretative guidance).
- (4) **Revision to Item 303(a)(3)(iv) (Results of Operations – Inflation and Price Changes)**, eliminating the express requirement to discuss the effects of inflation and instead encouraging companies “to focus on material information that is tailored to a company’s businesses, facts, and circumstances” (inflation and price changes may still need to be discussed if material).
- (5) **Revision to Item 303(a)(4) (Off-Balance Sheet Arrangements)**, now requiring companies “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 such [company’s] financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, cash requirements, or capital resources even when the arrangement results in no obligation being reported in the [company’s] consolidated balance sheets.”
- (6) **Revision to Item 303(a)(5) (Contractual Obligations) and Revised Item 303(b)(1) (Liquidity and Capital Resources)**, eliminating the currently required contractual obligations table and instead requiring discussion of material contractual obligations as part of the company’s discussion of its liquidity and capital resources. Smaller reporting companies, in particular, should note that material cash requirements from contractual and other obligations will need to be discussed in MD&A, without an exception for smaller reporting companies that were already not required to include a contractual obligations table. Note also that liquidity disclosures are required on both a short-term (up to 12 months) and long-term (more than 12 months into the future) basis.
- (7) **Revised Item 303(b) (Material Changes in Results of Operations Line Items)**, codifying the SEC’s existing interpretative guidance requiring disclosure of the underlying drivers for the changes, including when material changes within a line item offset one another (segment, product line and geographical information may also be required if material).
- (8) **Revision to Item 303(b)(2)(iii) (Net Sales and Revenues)**, now requiring narrative discussion of material changes in net sales and revenues, including underlying drivers (qualitatively and quantitatively).
- (9) **New Item 303(b)(3) (Critical Accounting Estimates)**, now requiring disclosure of critical accounting

estimates, changes in estimates, sensitivity disclosure, and related assumptions and uncertainties.

- (10) **Revision to Item 303(b) (Interim Periods)**, permitting some flexibility in the comparison of interim periods by now allowing companies to compare their most recently completed fiscal quarter to either the corresponding quarter of the prior year (as required in the past) or to the immediately preceding fiscal quarter. If the comparison is to the immediately preceding fiscal quarter, summary financial information for that quarter is required, either by directly including it in the filing or identifying the prior report where such information was provided. Similarly, if the company changes the period used for comparison, comparisons to both periods and the reasons for the change are required.

Compliance Date

The amended rule becomes effective on February 10, 2021. Companies are required to comply with these MD&A and financial disclosure amendments beginning with the first fiscal year that ends on or after the date that is 210 days after publication in the *Federal Register* (that is, for the fiscal year that ends after August 9, 2021). As such, December 31 year-end companies will not be required to comply with the amended rules until 2022. Early voluntary compliance is permitted after the effective date as long as the company complies with the amended disclosure item in its entirety and in all applicable filings going forward.

SEC Rule Amendments to Business Description, Legal Proceedings and Risk Factor Disclosures Under Regulation S-K

On August 26, 2020, the SEC adopted a [Final Rule to amend and modernize certain disclosure requirements under Regulation S-K](#) applicable to the description of business (Item 101), legal proceedings (Item 103) and risk factors (Item 105). The amendments became effective on November 9, 2020, and companies should update their annual reports on Form 10-K, as necessary, paying particular attention to the sections relating to the company's business strategy, human capital, risk factor categories and government regulation disclosures. Disclosures regarding human capital management may be

particularly challenging, with early filers adopting a variety of approaches to date. For more information about these changes, see our [October 2020](#) edition of *Securities Quarterly Update*.

COVID-19 Disclosure Considerations

In our [April 2020](#), [July 2020](#) and [October 2020](#) editions of *Securities Quarterly Update*, we reviewed various disclosure considerations and SEC guidance (including [CF Disclosure Guidance Topic No. 9](#) and [CF Disclosure Guidance: Topic No. 9A](#)) relating to COVID-19. What may have once been considered short-term impacts of COVID-19 may now reflect permanent costs of doing business, and given the continuing effects of COVID-19 on companies and markets, most or all of these considerations still apply and should again be considered and prior disclosures (including trends) reviewed and updated, as necessary.

SEC Enforcement Action Regarding Allegedly Inadequate COVID-19 Disclosure

On December 4, 2020, the [SEC announced that it settled charges in its first enforcement action](#) relating to a public company's allegedly inadequate and misleading disclosure as to the financial impacts of the COVID-19 pandemic. Although the settlement amount is relatively minor, the action is a reminder for public companies to assess and review COVID-19 disclosures carefully, integrating all related communications into the company's disclosure controls and procedures to permit for timely reporting, among other things, as more is likely to come in the enforcement area.

Reminder Regarding Changes to "Accelerated" and "Large Accelerated" Filer Definitions Potentially Impacting Filing Deadlines; New Cover Page Check Box

Forms 10-K filed in 2021 will be required to include an additional check box on the cover page, indicating whether an auditor assessment of the effectiveness of internal control is required.

As discussed in our [July 2020](#) edition of *Securities Quarterly Update*, the SEC adopted amendments to the "accelerated

filer” and “large accelerated filer” definitions, which, among other things, exclude from these definitions “smaller reporting companies” that had annual revenues of less than \$100 million in the last fiscal year. The amendments became effective on April 27, 2020, and apply to the annual reports on Form 10-K due on or after that date.

The company’s status as a “non-accelerated filer,” an “accelerated filer” or a “large accelerated filer” (determined at the end of the fiscal year using the second quarter end non-affiliate public float calculations) determines the company’s filing deadlines for periodic reports, with non-accelerated filers enjoying longer time frames. A company with a December 31 fiscal year end retained its current status until the end of 2020 and will reflect any change in its filer status on its annual report on Form 10-K to be filed in 2021. The amendments further increase the thresholds for exiting “accelerated” and “large accelerated” filer status and create more complexity by adding a revenue test to the exit thresholds.

Most significantly, as a result of these amendments, some smaller public companies will no longer be required to provide the SOX 404(b) auditor assessment of the effectiveness of internal control over financial reporting. Management’s report on the effectiveness of internal control over financial reporting will still be required.

Note that companies with non-affiliate public floats between \$75 million and \$250 million remain subject to all of the accelerated filer requirements unless their annual revenues are less than \$100 million.

Inline XBRL Reminder

Pursuant to the SEC’s [Phase-In of the Inline XBRL Requirements](#), accelerated filers that prepare their financial statements in accordance with U.S. GAAP are required to comply with Inline XBRL in reports for fiscal periods ending on or after **June 15, 2020**, and non-accelerated filers will be required to comply with Inline XBRL requirements for fiscal periods ending on or after **June 15, 2021**. Companies should update the Form 10-K exhibit index accordingly and remember to tag cover pages of subsequently filed current reports on Form 8-K (also including Exhibit 104 referencing

Inline XBRL tags on the cover page, which is required if any other exhibits are being filed with the Form 8-K).

SEC Rule Amendments to Regulation S-T and EDGAR Filer Manual – Electronic Signature Consent

On November 17, 2020, the SEC announced its adoption of a [Final Rule to amend Regulation S-T and the EDGAR Filer Manual](#), specifically amending Rule 302(b) to eliminate the previous requirement for executing and retaining for five years manual signature pages to SEC filings (including Forms 10-K/Q, Forms 8-K, Schedules 13D/G, and Forms 3, 4 and 5) and instead permitting electronic signatures as long as certain procedures are followed. These amendments became effective on December 4, 2020.

As an initial matter, before an electronic signature is first used to sign an SEC filing, the signatory is required to manually sign a consent agreeing that the use of an electronic signature in any SEC filing constitutes the legal equivalent of such individual’s manual signature for purposes of authenticating the signature to any filing for which it is provided. This consent is required to be retained for at least seven years after the date of the last electronically signed filing and shall be furnished to the SEC if so requested.

Pursuant to these amendments, SEC filings can now be signed either manually or electronically, signatures are still required to be obtained before a filing is made, and signatures can now be retained electronically.

Note, however, that to utilize electronic signatures, the amendments impose certain procedures. A platform that is used for electronic signatures (e.g., DocuSign) must require the signatory to present a physical, logical or digital credential that authenticates the signatory’s individual identity, reasonably provide for non-repudiation of the signature, provide that the signature be attached, affixed or otherwise logically associated with the signature page or document being signed, and must include a timestamp to record the date and time of the signature.

SEC Rule Amendments to Regulation S-X for Financial Disclosures About Acquired and Disposed Businesses

On December 30, 2020, the SEC's [Small Entity Compliance Guide](#) has been amended to reflect recent amendments to the significance tests in the definition of "significant subsidiary" and the financial disclosure requirements in Regulation S-X for acquisitions and dispositions of businesses.

SEC Modernizes the Accredited Investor and Qualified Institutional Buyer Definitions

On August 26, 2020, the [SEC announced amendments to the accredited investor and qualified institutional buyers definitions](#), to expand the criteria for qualifying as an "accredited investor" in Rule 501(a) of the Securities Act and "qualified institutional buyer" in Rule 144A. For more information, see our [October 2020](#) edition of *Securities Quarterly Update*.

SEC Rule Amendments Harmonizing "Patchwork" Exempt Offering Framework

On November 2, 2020, the SEC [announced its adoption of amendments to rules under the Securities Act of 1933, as amended](#), in an effort to harmonize registration exemptions. The amendments "(i)[e]stablish more clearly, in one broadly applicable rule, the ability of issuers to move from one exemption to another, (ii) increase the offering limits for Regulation A, Regulation Crowdfunding, and Rule 504 offerings, and revise certain individual investment limits, (iii) set clear and consistent rules governing certain offering communications, including permitting certain "test-the-waters" and "demo day" activities, and (iv) harmonize certain disclosure and eligibility requirements and bad actor disqualification provisions." Changes to the offering integration framework may be of interest to public companies.

SEC Final Rules for Disclosure of Payments by Resource Extraction Companies

On December 16, 2020, as part of the Dodd-Frank rule-making, the [SEC announced its adoption of final rules requiring resource extraction companies to disclose](#)

[payments made to the U.S. or foreign governments for the commercial development of oil, natural gas, or minerals.](#)

The rule becomes effective 60 days after publication in the *Federal Register* and provides for a two-year transition period. After the transition period, those companies that are subject to the rule will be required annually to submit Form SD no later than 270 days following the end of their most recently completed fiscal year.

SEC Proposed Rules

SEC Proposes Amendments to Rule 144

On December 22, 2020, the SEC [announced proposed amendments to Rule 144 under the Securities Act of 1933](#), as amended, to (i) revise the holding period determination for securities acquired upon the conversion or exchange of certain "market-adjustable securities" (proposing to eliminate "tacking" for securities acquired upon the conversion or exchange of the market-adjustable securities of a company that does not have a class of securities listed on a national securities exchange), (ii) require that a Form 144 be filed electronically and not in paper form, (iii) eliminate the Form 144 filing requirement related to the sale of securities of non-SEC reporting companies, (iv) amend the Form 144 filing deadline to correspond with the Form 4 filing deadline; and (v) amend Forms 4 and 5 to add an optional checkbox to indicate that a transaction being reported was intended to satisfy Rule 10b5-1(c) (affirmative defense in insider trading cases). The proposed amendments are subject to a 60-day public comment period.

SEC Proposes Amendments to Form S-8 Registration Statement and Rule 701 (Compensatory Equity Issuances)

On November 24, 2020, the [SEC announced proposed amendments to Form S-8 \(covering equity plan registration statements\) and Securities Act Rule 701 \(covering compensatory equity issuances by non-reporting companies\)](#). Some of the proposed amendments would (i) clarify the company's ability to register, and to allocate securities among, multiple incentive plans on a single Form S-8, (ii) allow companies to add additional securities to Form S-8 by automatically effective post-effective amendment, and (iii) make some changes to share counting

and payment of registration fees. Among other things, the proposed amendments to Rule 701 would increase the exemption limits and revise disclosure requirements. For both Rule 701 and Form S-8, the proposed amendments would somewhat expand (i) consultant and advisor eligibility to entities and (ii) former employee eligibility as to specified post-termination grants (as well as eligibility of former employees of acquired entities). The proposed amendments are subject to a 60-day public comment period.

SEC Proposes Temporary (Five-Year) Rules to Allow Participation by Certain “Platform Workers” (or “Gig Workers”) in Compensatory Offerings Under Rule 701 and Form S-8

On November 24, 2020, the SEC [announced proposed amendments to Rule 701](#) and Form S-8 that, “on a temporary basis and subject to percentage limits (no more than 15% of annual compensation), dollar limits (no more than \$75,000 in three years) and other conditions, would permit [a company] to provide equity compensation to certain “platform workers” who provide services [but not goods] available through the [company’s] technology-based platform or system.” The proposed amendments are subject to a 60-day public comment period.

FOR MORE INFORMATION

For more information, please contact [a member of our Corporate Transactions & Securities group](#).

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