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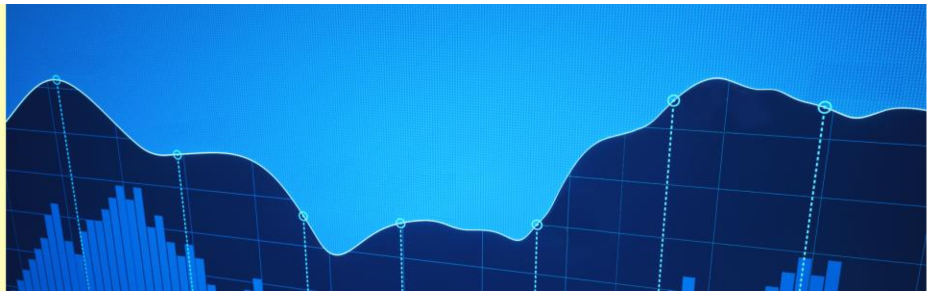

Securities Quarterly Update

January 2024 | 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 recent SEC developments affecting Form 10-K, proxy statements, and other SEC filings; and potential SEC rule changes.*

Recent Developments

Below is a discussion of certain select areas of recent developments by the Securities and Exchange Commission (SEC) and stock exchanges during 2023 and late 2022, which public companies should consider when preparing their Form 10-K, proxy statements, and other SEC filings.

Cybersecurity Disclosures

In July 2023, the SEC adopted final rules requiring certain cybersecurity-related disclosures intended to "enhance and standardize disclosures regarding cybersecurity risk management, strategy, governance, and incidents by public companies." These rules require that public companies provide cybersecurity-related disclosure in annual reports on Form 10-K and report material cybersecurity incidents on Form 8-K. Companies should review their risk factor and other existing cyber-related disclosures for consistency with the new Item 1C disclosure in the Form 10-K and take another look at proxy disclosures relating to the board's oversight of cybersecurity (and artificial intelligence, if applicable) and related director qualifications. Behind the scenes, some work may still need to be done on cybersecurity policies, incident response plans, materiality assessments, and disclosure controls and procedures to be ready for additional scrutiny from the public and regulators. For additional information, see our alert dated July 27, 2023 and our alert dated December 11, 2023.

Clawback Policies

In June 2023, the SEC approved the new listing standards proposed by NYSE and Nasdaq, which require listed companies to adopt a written clawback policy; failure to do so or to enforce any required clawback could result in delisting from the stock exchange. The policy will be required to be filed as an exhibit to Form 10-K. The Form 10-K cover page includes additional checkboxes and additional disclosures would be required if a clawback is triggered. Proxy statement disclosures related to clawback policies may also require some modification. For more information, see our alert dated September 29, 2023 and our alert dated November 8, 2022.

Rule 10b5-1 Trading Plans and Insider Trading Policies

In December 2022, the SEC adopted final rules relating to Rule 10b5-1 insider stock trading plans, company insider trading policies and procedures, and certain equity grants. As a result of these rules, many public companies reviewed and revised their insider trading policies and procedures, updated their D&O questionnaires, and reassessed their option grant practices. The insider trading policy will be required to be filed as an exhibit to Form 10-K. Some discussion may also be included in proxy disclosures. See our alert dated December 15, 2022 for more information.

Share Repurchase Rule

In May 2023, the SEC adopted a share repurchase rule that, among other things, would have required quarterly reporting of daily repurchase transactions. See our alert dated May 3, 2023 for more information. The U.S. Court of Appeals for the Fifth Circuit vacated the rule in December 2023, but the SEC may decide to repropose the rule. In the meantime, public companies are only required to provide Form 10-K/10-Q repurchase disclosures under the SEC's old rules.

Other Considerations

As always, risk factor disclosures should be updated for company, industry, and general developments, with accompanying updates to forward-looking statements. MD&A may be impacted by recent trends and/or changes in company strategic direction. For most companies, COVID-19 disclosures can likely be significantly pulled back or eliminated. When updating exhibit indexes, remember new exhibit requirements and consider if a securities description exhibit needs any updates. Non-GAAP financial measures and key performance indicators may be worth another look. There has been some recent SEC scrutiny on perks, Section 16 controls and procedures, and related party disclosures. Sustainability; environmental, social, and governance (ESG); and diversity, equity, and inclusion (DEI) disclosures may also merit another review given recent litigation and greenwashing claims, and human capital/talent management disclosures tend to be evolving, especially as we await additional SEC rulemaking on human capital and climate.

In January 2024, the SEC's Division of Corporation Finance posted an updated version of CF Disclosure Guidance: Topic No. 7, Confidential Treatment Applications Submitted Pursuant to Rules 406 and 24b-2. The updated information includes guidance with respect to options for confidential treatment orders that are about to expire.

Please further note that the SEC has expanded XBRL and inline XBRL requirements for various types of disclosure, including with respect to the above-discussed topics of cybersecurity, clawbacks, and Rule 10b5-1 plans. See our alerts linked above for additional information. Companies should discuss with their filing agent well in advance of filing to determine how much time will be required to complete the XBRL tagging.

Regulatory Focus Areas

Cash Flow Disclosures

Among the areas on which the SEC focused in 2023 was the statement of cash flows in public company financial statements. In December 2023, SEC Chief Accountant Paul Munter reminded companies and their auditors that the statement of cash flows "has consistently been a lead area of restatements" and stressed "the importance of performing an objective analysis from the perspective of a reasonable investor when evaluating the materiality of both the financial statement and ICFR impacts of an error in the statement of cash flows, including the significance of the statement of cash flows to the investor's complete understanding of the financial condition of the company." In the context of considering whether errors in the statement of cash flows constitute a material error in prior periods requiring a restatement of financial statements, when "presented with analyses that conclude an error in the statement of cash flows is not material because it is an error in classification only," the SEC Office of the Chief Accountant "[has] not found such analyses and their corresponding arguments persuasive since classification itself is the foundation of the statement of cash flows."

The Chief Accountant's statement includes some suggestions for additional disaggregation of amounts included in the statement of cash flows and for supplements with disclosure of noncash investing and financing activities. The statement also reiterates the expectation to disclose significant account policies that materially affect the determination of cash flow classification and emphasizes the importance of internal controls related to such classification as well as the disclosure of noncash items. Further, audit procedures are expected to be specifically responsive to risks in the statement of cash flows rather simply reconciling to other financial statements.

Revenue Recognition

The SEC also continues its enforcement activities relating to improper timing of revenue recognition. For example, in June 2023, the SEC issued an order charging a company with improper revenue recognition that led to an overstatement of revenue in the company's financial statements and a resulting restatement of the financial statements. Consider periodically revisiting revenue recognition and disclosure controls.

Other Focus Areas

In recent comment letters, the SEC sent climate-related comments to numerous large companies, including asking companies to explain discrepancies between the disclosures in their sustainability reports and the disclosures in their SEC filings. Such comments are similar to those in the SEC's sample letter issued in September 2021. In light of this scrutiny, public companies should evaluate their climate-related disclosures as a whole and ensure that any necessary climate-related disclosure is included in the relevant SEC filings.

Certain "large traders" and broker-dealers are required to comply with Section 13(h) of the Securities Exchange Act of 1934 and Exchange Act Rule 13h-1. In July 2023, the SEC settled an enforcement action relating to a purported violation of such rules, which resulted in a penalty of over $1 million. Accordingly, large traders and broker-dealers should evaluate which requirements are applicable to their business and take steps to ensure compliance.

Anticipated SEC Rule Changes

The SEC is considering a number of rules, including rulemaking related to ESG issues.

One of the more closely watched proposals relates to climate change disclosure. The SEC's final climate disclosure rule is currently tentatively scheduled for April 2024, and it remains unclear what shape it would take, particularly as it relates to potential disclosure of scope 3 (indirect) greenhouse gas emissions and climate-related metrics in the financial statement line items. On the state level, perhaps most significantly, California passed two bills relating to climate risk and emissions disclosures that could impact thousands of companies doing business in the state. The Climate-Related Financial Risk Act will require certain companies to report biennially on climate-related financial risk, and the Climate Corporate Data Accountability Act will require certain companies to publicly disclose their scope 1, 2, and 3 greenhouse gas emissions. See our alert dated September 15, 2023 for additional information.

In September 2023, the SEC's Investor Advisory Committee recommended that the SEC adopt rules requiring public companies to disclose additional information related to their human capital resources. Such rules have not yet been proposed by the SEC, but rulemaking in this area is expected and may include additional DEI statistics and workforce turnover metrics.

FOR MORE INFORMATION

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