

Capital Markets

Skadden

2020 Capital Markets Regulatory Review

The tables below provide an overview of some of the key capital markets and corporate governance reforms that have taken effect in 2020 or are poised to take effect in 2021. These regulatory- and guidance-related developments relate to disclosure, filing and technical requirements, and substantive offering and corporate governance reforms.

Disclosure Requirements

General Development of Business (Item 101 (a)) Regulation S-K)

[Adopting Release](#)

- Eliminates the five-year look-back in favor of disclosing material developments divorced from a specific time frame.
- A principles-based materiality disclosure framework replaces the requirement to discuss prescribed topics regardless of materiality.
- Hyperlinks to past disclosure are permitted; companies may supplement future reports with only material developments.

Practical Effect:

- Does not apply to foreign private issuers (FPIs), unless they elect to use U.S. forms that reference the appropriate item.
- Elicits highly tailored narratives that may lead to more disclosure divergence in among differently situated companies.

Effective Date:

Mandatory compliance required as of November 9, 2020.

More Analysis:

[SEC Modernizes Business Description, Legal Proceedings and Risk Factors Disclosure Requirements](#)

Business Description (Item 101(c) Regulation S-K)

[Adopting Release](#)

- Requires human capital resources disclosures to the extent such disclosures are material to an understanding of the business. Companies must disclose both the number of employees and other material factors.
- Companies must disclose the material impact of complying with government regulations (where previously only environmental regulations were required).
- Amendments provide examples of potential disclosures emphasizing an issuer-specific, tailored assessment of materiality.

Practical Effect:

- Does not apply to FPIs, unless they elect to use U.S. forms that reference the appropriate item.
- The human capital disclosure requirement highlights the growing prominence of environmental, social and governance (ESG)-related disclosures, but apart from the obligation to disclose the number of employees, the requirement remains broadly nebulous and principles-based, rather than prescriptive.

Effective Date:

Mandatory compliance required as of November 9, 2020.

More Analysis:

[SEC Modernizes Business Description, Legal Proceedings and Risk Factors Disclosure Requirements](#)

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Legal Proceedings

(Item 103 Regulation S-K)

[Adopting Release](#)

- Imposes higher monetary threshold for disclosure of certain environmental proceedings resulting in sanctions (\$100,000 to \$300,000); companies may opt for a different, materiality-based threshold not to exceed \$1 million.
- Hyperlinks or cross-references to legal proceedings disclosure elsewhere in the document are permitted to avoid duplication.

Practical Effect:

- Does not apply to FPIs, unless they elect to use U.S. forms that reference the appropriate item.

Effective Date:

Mandatory compliance required as of November 9, 2020.

More Analysis:

[SEC Modernizes Business Description, Legal Proceedings and Risk Factors Disclosure Requirements](#)

Risk Factors/ Risk Factor Summary

(Item 105 Regulation S-K)

[Adopting Release](#)

- If risk factors exceed 15 pages, issuers must include a bulleted risk factor summary not to exceed two pages.
- Headings are required in sections to group similar risk types.
- Boilerplate risk factors now fall under a “General Risk Factors” heading.
- Issuers must disclose “material” as opposed to the “most significant” risk factors.

Practical Effect:

- Applies to domestic issuers, as well as foreign private issuers using forms F-1, F-3 or F-4.
- Amendments target shorter, more meaningful risk factors over a “kitchen sink approach.”
- Deprioritizes nontailored risk factors by grouping them together.

Effective Date:

Mandatory compliance required as of November 9, 2020.

More Analysis:

[SEC Modernizes Business Description, Legal Proceedings and Risk Factors Disclosure Requirements](#)

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Acquisitions and Dispositions

(Rule 3-05 and Article 11 of Regulation S-X)

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- Updates the Investment Test and Income Test, used to determine significance, and increases the thresholds a target must hit to be deemed significant.
- The revised rules also typically require fewer years of financial statements for acquisitions/dispositions at various levels of significance, with a ceiling of two instead of three years of audited financial statements.
- Once target business has been consolidated in an issuer's audited financials for the requisite period, not to exceed one fiscal year, separate financials will cease to be required.
- Permits abbreviated financial statements if a target was carved out of larger entity and did not maintain separate financials.
- Issuers have greater scope to use *pro forma* information to determine significance. *Pro forma* details are now subject to Transaction Accounting Adjustments and Autonomous Entity Adjustments.

Practical Effect:

- Does not apply to target company financial statements required to be provided on Form S-4 or F-4, but will apply to *pro forma* information included therein.
- Expected to reduce issuer compliance burden.

Effective Date:

Voluntary compliance is currently permitted.

Mandatory compliance required as of January 1, 2021.

More Analysis:

[SEC Adopts Changes to Financial Disclosure Requirements for Acquisitions and Dispositions](#)

Guarantor Financial Statements

(Article 13, Rules 3-10, 13-01 and 13-02 Regulation S-X)

Adopting Release

- Replaces onerous requirements in registered offerings that guarantors and affiliates whose securities collateralize the issuer's provide full audited annual and interim financials, or in certain cases, "abbreviated disclosures," both of which can be complex and time-consuming. The parent company also is subject to "alternative disclosures" for as long as guaranteed securities are outstanding.
- Revised rules make it easier to omit full financials and qualify for alternative disclosures, and reduce the preparation burden of "summarized financial information." New disclosures are both financial and nonfinancial in nature.

Practical Effect:

- Amendments provide more incentive for issuers to consider registered offerings, as opposed to private-for-life transactions.
- The update should reduce the time and cost requirements of disclosure document preparation.
- Exhibit 22 is required (Item 601(b)(22) of Regulation S-K), listing each affiliate whose securities are pledged as collateral for registered securities.

Effective Date:

Voluntary compliance is currently permitted.

Mandatory compliance required as of January 4, 2021.

More Analysis:

[SEC Adopts Amendments to Rules 3-10 and 3-16 of Regulation S-X in Certain Registered Debt Offerings](#)

¹ The amendments revise Rules 3-10 and 3-16 of Regulation S-X, and relocate part of Rule 3-10 and all of Rule 3-16 to the new Article 13 in Regulation S-X, which is comprised of new Rules 13-01 and 13-02.

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Selected Financial Data (MD&A) (Item 301 Regulation S-K)

[Adopting Release](#)

- Eliminates the requirement that issuers disclose “selected financial data” for the past five years.

Practical Effect:

- Eliminating the need to provide five years of financial statements (or restatements) should realize reduced compliance costs.
- Issuer should focus instead on known trends or uncertainties that, in management’s assessment, are reasonably likely to have a material impact on net sales, revenues or income from continuing operations.
- The SEC commented that a material trends disclosure that extends five years or beyond, though not required, may be helpful for investors.

Effective Date:

Voluntary compliance will be permitted 30 days after publication in the Federal Register (likely early 2021).

Mandatory compliance is required as of the first fiscal year ending on or after the date that is 210 days after publication in the Federal Register. (For most calendar year-end companies, compliance will first be required on annual reports for fiscal year ending December 31, 2021.)

More Analysis:

[SEC Amends MD&A and Other Financial Disclosure Requirements](#)

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Supplemental Financial Information (MD&A)

(Item 302 Regulation S-K)

Adopting Release

- The requirement that companies present at least two years of quarterly financial metrics has been eliminated/streamlined, depending on circumstances.
- Companies are only required to present supplementary financial information when one or more material retrospective changes occurs to financial statements for the most recent two-year period.
- Issuers must explain the reasons for the material changes and include summarized financial information and earnings per share.

Practical Effect:

- To the extent disclosure is required, the amendments place more emphasis on material retrospective changes, the reasons they occurred and their effect on the quarterly periods affected.

Effective Date:

Voluntary compliance will be permitted 30 days after publication in the Federal Register (likely early 2021).

Mandatory compliance is required as of the first fiscal year ending on or after the date that is 210 days after publication in the Federal Register. (For most calendar year-end companies, compliance will first be required on annual reports for fiscal year ending December 31, 2021.)

More Analysis:

[SEC Amends MD&A and Other Financial Disclosure Requirements](#)

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Contractual Obligations Table/Material Cash Requirements (MD&A)

(Items 303(a)(5) and 303 (b)(1) Regulation S-K)

[Adopting Release](#)

- The contractual obligations table requirement has been eliminated.
- In place of a table, issuers are required to disclose material cash requirements generally, including for capital expenditures and known contractual requirements.
- Material cash disclosure should include the general purpose of the cash requirement and anticipated funding source.

Practical Effect:

- Considerable cost and time savings are projected for issuers, who will no longer have to disclose every contract in tabular form, regardless of materiality.

Effective Date:

Voluntary compliance will be permitted 30 days after publication in the Federal Register (likely early 2021).

Mandatory compliance is required as of the first fiscal year ending on or after the date that is 210 days after publication in the Federal Register. (For most calendar year-end companies, compliance will first be required on annual reports for fiscal year ending December 31, 2021.)

More Analysis:

[SEC Amends MD&A and Other Financial Disclosure Requirements](#)

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Critical Accounting Estimates (MD&A)

(Item 303(b)(3) Regulation S-K)

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- Issuers must disclose accounting estimates that materially affect reported financial information.
- The issuer should provide the qualitative and quantitative information necessary to understand estimation uncertainty and the impact of the estimate on the issuer's financial condition or results of operations.

Practical Effect:

- The amendments largely codify existing SEC guidance in effect since 2003.

Effective Date:

Voluntary compliance is permitted 30 days after publication in the Federal Register (likely early 2021).

Mandatory compliance is required as of the first fiscal year ending on or after the date that is 210 days after publication in the Federal Register. (For most calendar year-end companies, compliance will first be required on annual reports for fiscal year ending December 31, 2021.)

More Analysis:

[SEC Amends MD&A and Other Financial Disclosure Requirements](#)

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MD&A Disclosure Objectives

(Item 303 Regulation S-K)

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- Clarifies the overall objective of the MD&A and emphasizes principles-based disclosure, while deemphasizing prescriptive “tick-mark” requirements.

Practical Effect:

- SEC staff has emphasized the importance of representing management’s perception of the company and the need for tailored, company-specific disclosures.
- Specific examples of more principles-based reporting include the elimination of the requirement to disclose inflation and price changes unless they are material.
- Issuers may also tailor their disclosure, *e.g.*, by choosing whether to compare the most recently completed quarter with the corresponding quarter of the prior year, or with the immediately preceding quarter.

Effective Date:

Voluntary compliance is permitted 30 days after publication in the Federal Register (likely early 2021).

Mandatory compliance is required as of the first fiscal year ending on or after the date that is 210 days after publication in the Federal Register. (For most calendar year-end companies, compliance will first be required on annual reports for fiscal year ending December 31, 2021.)

More Analysis:

[SEC Amends MD&A and Other Financial Disclosure Requirements](#)

Filing/Technical Requirements

Accelerated Filer/Large Accelerated Filer Definitions

(Rule 12b-2 Exchange Act)

Adopting Release

- Excludes from the definition of accelerated filers smaller reporting companies (SRCs) with revenues under \$100 million in their most recent fiscal year.
- Increases thresholds for qualifying and exiting accelerated and large accelerated filer status.

Practical Effect:

- SRCs do not need auditor attestation of internal controls over financial reporting, reducing the compliance burden for smaller companies.
- A checkbox has been added to cover pages of Forms 10-K, 20-F and 40-F to indicate whether auditor attestation of internal control of financial reporting is included.
- Companies must calculate new transition and exit thresholds.
- Companies should assess applicable filing requirement changes upon a change in status.

Effective Date:

Mandatory compliance required as of April 27, 2020.

More Analysis:

[SEC Adopts Amendments to the Accelerated Filer and Large Accelerated Filer Definitions](#)

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Electronic Signatures

(Rule 302(b) of Regulation S-T)

[Adopting Release](#)

- The current requirement that electronic filings be manually signed via signature authentication document has been replaced.
- Electronic signatures are permitted subject to certain requirements set forth in the EDGAR Filer Manual and Regulation S-T.
- Prior to e-signing, individuals must first manually sign an authentication document agreeing to legal equivalence of electronic and manual signatures going forward.

Practical Effect:

- Companies transitioning to electronic signatures must establish internal and recordkeeping procedures to maintain both an electronic or hard copy of the signatory's manually signed authentication document (seven years) and electronic copies of signature authentication documents (five years).

Effective Date:

Voluntary compliance is currently permitted.

Mandatory compliance required as of December 4, 2020 (note that manual signatures are still permitted).

More Analysis:

[SEC Adopts Rules To Allow Use of Electronic Signatures](#)

Inline XBRL Requirements

[Adopting Release](#)

- Cover pages need to be tagged with inline eXtensible Business Reporting Language (XBRL).

Practical Effect:

- Non-Accelerated Filers must begin complying with XBRL requirements, as outlined in the three-year phased adoption.

Effective Date:

Mandatory compliance for:

- Large Accelerated Filers: Required as of June 15, 2019.
- Accelerated Filers: Required as of June 15, 2020.
- Non-Accelerated Filers: Required as of June 15, 2021.

More Analysis:

[SEC Modernizes and Simplifies Disclosure and Compliance Requirements](#)

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Offering Reform

Expansion of Accredited Investor Definition

(Rule 215 and Rule 501(a) of Regulation D)

[Adopting Release](#) (expanding the definition of accredited investor)

[Adopting release](#) (permitting an issuer under Rule 506(c) an offer to rely on prior investor verification for five years)

- Permits more investors to qualify as accredited by 1) recognizing certain professional certifications, designations or credentials as proof of sufficient investor sophistication; 2) permitting knowledgeable employees of private funds to qualify; and 3) recognizing new entity types as accredited investors, provided certain requirements are met.

Practical Effect:

- Expands the category of individuals and entities that qualify as accredited investors and reduces the burden on issuers to verify accredited investor status.
- The SEC has stated it may recognize additional professional certifications as accredited investors in the future.

Effective Date:

Permitted as of December 8, 2020.

More Analysis:

[SEC Expands Accredited Investor Definition To Allow More Participation in Private Offerings](#)

[SEC Adopts Amendments to Exempt Offering Framework](#)

Updating Integration Framework/Facilitating Exempt Offerings

(Securities Act Rules 152, 241)

[Adopting Release](#)

- Moves away from the unclear five-factor integration test in favor of an assessment focusing on facts and circumstances with some bright-line safe harbors.
- Specific safe harbors include offers that are more than 30 days apart and offers that are made in reliance on Rule 701 (employee benefit plan) or via Regulation S. Offers made in reliance on an exemption that permits general solicitation will not be integrated with a previous terminated or completed offering.
- The maximum size of certain exempt offerings has been raised and investment limits have been increased or eliminated.
- Expands permitted exempt offering communications, such as demo day and testing-the-waters communications.

Practical Effect:

- Increases the attractiveness and decreases the risk of exempt offerings, while making the exempt offering framework more cohesive.
- Note that issuers should be clear of new requirements. For example, the new rules permit generic solicitations of interest (instead of restricting solicitations to sophisticated purchasers), without settling on a particular exemption, but general solicitation would foreclose the availability of certain exemptions.

Effective Date:

Mandatory compliance required as of 60 days after publication in the Federal Register, with the exception of the extension of temporary Regulation Crowdfunding regulations, which will go into effect upon publication in the Federal Register.

More Analysis:

[SEC Adopts Amendments to Exempt Offering Framework](#)

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Corporate Governance

Virtual Shareholder Meetings

[Staff Guidance for Conducting Shareholder Meetings in Light of COVID-19 Concerns](#)

- As a result of the COVID-19 pandemic, many companies are holding all-virtual shareholder meetings.
- Delaware law permits virtual shareholder meetings. Other states, such as New York and New Jersey, do not normally permit them, but have granted temporary emergency relief to allow them.
- The SEC has provided guidance regarding logistics and disclosure considerations for virtual meetings.

Practical Effect:

- Virtual shareholder meetings are likely to be an ongoing consideration in the 2021 proxy season. Companies should monitor changes in regulatory developments, proxy advisory recommendations, the state of the pandemic and the considerable logistical concerns implicated by a virtual meeting.

Effective Date:

In effect, but subject to change.

More Analysis:

[Planning Ahead: Virtual Shareholder Meetings in the 2021 Proxy Season](#)

[Delaware Governor Issues Order Regarding Notice of Change to Virtual Stockholders' Meeting for Public Companies Due to COVID-19](#)

Shareholder Proposals

[\(Securities Exchange Act Rule 14a-8\)](#)

[Adopting Release](#)

- Makes the requirements for submitting and resubmitting shareholder proposals more onerous, by: 1) requiring shareholders to have held securities of either greater value and/or for a longer period of time than previously; 2) requiring documentation when a proposal is submitted by a representative; 3) requiring a commitment by the proponent to be available to engage with the company, either shortly before or after the proposal is submitted; 4) limiting a representative (as well as a shareholder) to one proposal; and 5) making it more difficult to resubmit a failed proposal.

Practical Effect:

- Amendments are likely to reduce the volume of shareholder proposals received, especially by representatives, and ensures that shareholders have more economic stake in the company before they are able to submit proposals, incurring costs on behalf of all shareholders.

Effective Date:

The amendments will apply to proposals submitted for annual or special meetings held on or after January 1, 2022, which means that the new rules will not be relevant when analyzing proposals received for the upcoming 2021 proxy season.

More Analysis:

[SEC Adopts Amendments to Shareholder Approval Rules](#)

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Auditor Independence (Rule 2-01, Regulation S-X)

[Adopting Release](#)

- New rules relax independence standards when the auditor and audit client are entities under common control, are affiliates or are engaged in certain financial relationships, including mortgage, car and student loans.

Practical Effect:

- Reduces the situations in which auditors will not be considered independent, provides greater clarity to issuers and auditors, and aims to decrease audit costs.

Effective Date:

Voluntary compliance will be permitted upon publication in the Federal Register.

Mandatory compliance required as of 180 days after publication in the Federal Register.

More Analysis:

[SEC Adopts Amendments to Auditor Independence Rules](#)

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