

# SEC Proposes Amendments to, and Issues Interpretive Guidance on, Key Financial Disclosure Requirements; Chairman Clayton Issues Related Public Statement

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Last week, as part of its continued efforts to modernize and simplify disclosure requirements, the U.S. Securities and Exchange Commission (SEC) proposed amendments to financial disclosure requirements under Regulation S-K<sup>1</sup> and issued interpretive guidance on certain uses of key performance indicators and metrics.<sup>2</sup> In a related public statement, SEC Chairman Jay Clayton provided context for these changes and also addressed disclosure issues with respect to the recent coronavirus outbreak and environmental matters.<sup>3</sup>

## Proposed Amendments to Financial Disclosure Requirements

The SEC seeks to eliminate duplicative disclosures, modernize Item 303 of Regulation S-K (Management's Discussion & Analysis of Financial Condition and Results of Operations, or MD&A), and simplify compliance efforts for registrants. If adopted, the proposed amendments would eliminate Item 301 of Regulation S-K (Selected Financial Data) and Item 302 of Regulation S-K (Supplementary Financial Information). In addition, the proposed amendments would facilitate a principles-based approach to, and "modernize and enhance," MD&A disclosures. Highlights of the proposed MD&A amendments are described below.

**Objective.** Consolidating certain Instructions to current Item 303(a), a new Item 303(a) would set forth the objective of MD&A and outline the types of disclosures that should be included in MD&A, including material information relevant to an assessment of the financial condition and results of operations of the registrant, an evaluation of the amounts and certainty of cash flows from operations and outside sources, a narrative explanation of the financial statements that allows investors to view the registrant from management's perspective, and material events and uncertainties.

**Full fiscal years.** Current Item 303(a), which outlines disclosure requirements for full fiscal years, would be renumbered to Item 303(b) and include the following additional changes:

- "Product lines," similar to the current reference to "geographic areas," would be included as an example of a type of subdivision of the registrant's business that may require separate discussion.

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- When material to an understanding of the registrant's businesses as a whole, new Item 303(b) would also require a quantitative and qualitative description of the "underlying reasons" for material changes from period-to-period in one or more line items of the financial statements, including where material changes within a line item offset one another.
  - Consistent with prior SEC staff guidance, the proposed amendments would require broad disclosure of material cash requirements and commitments, as well as the anticipated sources of funds needed to satisfy such requirements.
  - Events that will or are *reasonably likely* to cause a material change in the relationship between costs and revenues would need to be disclosed.
  - The express reference to "inflation" would be eliminated.

**Interim Periods.** Current Item 303(b), which outlines disclosure requirements for interim periods, would be renumbered to Item 303(c) and allow registrants to compare their most recently completed quarter to either the corresponding quarter of the prior year (as currently required) or to the immediately preceding quarter. Any change in presentation would need to be explained.

**Off-balance sheet arrangements.** The current requirement in Item 303(a)(4) to discuss off-balance sheet arrangements would be replaced with a new instruction that would require 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 or changes therein.

**Tabular disclosure of contractual obligations.** The proposed rules would eliminate the requirement to provide tabular disclosure of contractual obligations under current Item 303(a)(5).

**Critical accounting estimates.** Consistent with prior SEC staff guidance, the proposed amendments would define, and require disclosure of, critical accounting estimates, including, to the extent material, why each critical accounting estimate is subject to uncertainty, how much each estimate has changed during the reporting period, and the sensitivity of the reported amount to the methods, assumptions, and estimates underlying its calculation.

## **Interpretive Guidance on Key Performance Indicators and Metrics in MD&A**

Current MD&A rules require a discussion and analysis of statistical data that, in a registrant's judgment, enhances a reader's understanding of the MD&A. The SEC recognizes that, given the widespread use by registrants of financial and non-financial metrics when describing the performance and status of their business – and the significant variance in metrics across companies and industries – an existing regulatory disclosure framework (such as rules pertaining to disclosure of non-GAAP financial measures) may apply, or investors may need additional information or context to understand the metric(s) presented. The SEC reminds registrants that it would generally expect the following disclosures to accompany any such metric, based on the facts and circumstances:

- a clear definition of the metric and how it is calculated;
- a statement indicating the reasons why the metric provides useful information to investors; and

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- a statement indicating how management uses the metric in managing or monitoring the performance of the business.

To the extent calculation or presentation methods of these indicators or metrics are changed from period to period, registrants should consider the need to disclose, among other things, the reasons for the changes. Finally, the SEC reminds registrants of the importance of maintaining effective disclosure controls and procedures around material key performance indicators or metrics to ensure consistency and accuracy.

## **Chairman Clayton Issues Public Statement on Proposed Amendments and Interpretive Guidance, Impact of the Coronavirus Outbreak and Environmental and Climate-Related Disclosure**

In tandem with the proposed rulemaking and interpretive guidance, SEC Chairman Jay Clayton issued a public statement citing the benefits of the same to investors and the capital markets.

He also addressed the uncertainty and potential disclosure issues surrounding the recent coronavirus outbreak in China, with cases identified in a growing number of international locations, including the United States. Recognizing that such effects may be difficult to assess, Chair Clayton has asked the SEC staff “to monitor and, to the extent necessary or appropriate, provide guidance and other assistance to issuers and other market participants regarding disclosures related to the current and potential effects of the coronavirus.”<sup>4</sup> Chair Clayton also noted that how issuers plan for the uncertainties associated with the coronavirus, and how they respond to related events, could be material to an investment decision.

Finally, Chair Clayton provided a summary of his prior discussions on the SEC’s ongoing work in the evolving and complex area of environmental and climate-related securities law disclosures. His summary touched on threshold issues in crafting and evaluating disclosure mandates and guidance on this topic, the SEC’s 2010 interpretive release, issuer and investor engagement efforts to date, and participation with non-U.S. regulators in international disclosure review initiatives, all to ensure that interested market participants have efficient access to this information.

## **Next Steps**

**Proposed Amendments.** Comments on the proposed amendments discussed above are due 60 days after publication in the Federal Register. Registrants should review the proposed rules, including the specific requests for comment in the proposing release, consider how the amendments, if adopted, would impact their disclosure, and determine whether to timely submit any comments to the SEC.

**Interpretive Guidance.** The interpretive guidance is effective for registrants upon publication in the Federal Register.

**Coronavirus/Environmental and Climate-Related Disclosure.** Registrants should assess their exposure to the current and potential effects of the coronavirus and, where material, consider how to address such exposure in their public disclosures. Registrants should also keep abreast of any updates or disclosure guidance from the SEC or SEC staff.

Read [here](#).

<sup>1</sup> See “*Management’s Discussion and Analysis, Selected Financial Data, and Supplementary Financial Information*,” SEC Release No. 33-10750 (Jan. 30, 2020), available at <https://www.sec.gov/rules/proposed/2020/33-10750.pdf>.

<sup>2</sup> See “*Commission Guidance on Management’s Discussion and Analysis of Financial Condition and Results of Operations*,” SEC Release No.

33-10751 (Jan. 30, 2020), available at <https://www.sec.gov/rules/interp/2020/33-10751.pdf>.

<sup>3</sup> See “*Proposed Amendments to Modernize and Enhance Financial Disclosures; Other Ongoing Disclosure Modernization Initiatives; Impact of the Coronavirus; Environmental and Climate-Related Disclosure*,” SEC Chairman Jay Clayton (Jan. 30, 2020), available at <https://www.sec.gov/news/public-statement/clayton-mda-2020-01-30> (hereinafter referred to as “Clayton Statement”).

<sup>4</sup> See Clayton Statement

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