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Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

2 January 2018

Re: Request for Comment on FAST Act Modernization and Simplification of Regulation S-K (Release No. 33-10425; 34-81851; IA-4791; IC-32858; File No. S7-08-17)

Dear Mr. Fields:

Ernst & Young LLP is pleased to provide comments to the Securities and Exchange Commission (SEC or Commission) on its proposal to modernize and simplify Regulation S-K in response to a mandate in the Fixing America's Surface Transportation Act (FAST Act).

We support the Commission's objective and believe that many of the proposed amendments are consistent with our prior recommendations.¹ While this proposal does not address Regulation S-K comprehensively, we encourage the Commission to make completing the disclosure effectiveness initiative and related rule-making projects a priority for the benefit of investors and other constituents in the financial reporting system.

Disclosure objectives and materiality in the context of securities laws and regulation

Certain of the proposed amendments would require registrants to consider whether a specified disclosure is material. We agree that the primary consideration for all disclosures should be their materiality, which is well defined in the federal securities laws. That is, materiality, in the context of federal securities laws and regulations, is generally understood to be determined based on whether a reasonable investor's judgments or conclusions about a company or its securities would be affected by the misstatement or omission of a particular disclosure, considering the total mix of information.

As we suggested in our 21 July 2016 letter to the SEC, articulating clear and understandable disclosure objectives in each item of Regulation S-K should help elicit more meaningful, complete and focused disclosure. There should be no need to embed quantitative bright-lines, or explicit materiality thresholds or references, within the respective disclosure requirements because materiality would be the overarching principle. We believe that the references to materiality in the proposed amendments (e.g., the proposed amendments to Instruction 1 of Item 303(a), which would require a registrant to

¹ Refer to our comment letters on the SEC's disclosure effectiveness initiative, including our 21 July 2016 comment letter on the SEC concept release on business and financial disclosures required by Regulation S-K (Release No. 33-10064; 34-77599; File No. S7-06-16).

consider whether the discussion of the earliest of the three periods covered in management's discussion and analysis (MD&A) would be "material to an understanding of the registrant's financial condition, changes in financial condition, and results of operations") could cause confusion and result in inconsistent application, as discussed below.

The appendix to this letter lists various references to "material," "materially" and "materiality" in the disclosure items of Regulation S-K. Overall, we identified 225 instances in Regulation S-K that refer to materiality in a context that in many cases is narrower than the total mix of information, such as *material to the investor or investment decision, material to the registrant's business and material to operating results or financial condition*. In many of these cases, it is unclear whether the SEC intended a registrant to evaluate materiality in a context different than the total mix of information. We recommend that the Commission reconsider the disclosure requirements, objectives and instructions in Regulation S-K to evaluate whether references to "material", or its derivations, can be avoided, unless it is the express intention of the Commission for registrants to apply the concept of materiality in a context different than its common application under federal securities law. Accordingly, as part of its broader review of Regulation S-K, we suggest that the Commission review the references to materiality in Regulation S-K outlined in the appendix to this letter (and other materiality references in the Regulation that we excluded from the scope of the appendix) and consider whether it would be appropriate to remove, modify or retain those references.

Management's discussion and analysis

The proposal would allow a registrant that includes three years of audited financial statements in its filing to omit the discussion of the earliest of the three years if such discussion (1) is not material to an understanding of its financial condition, changes in financial condition and results of operations and (2) has been included in the registrant's prior-year Form 10-K. In addition, the proposed instruction would no longer refer to two successive year-to-year comparisons, which many registrants have previously filed. We support the proposed changes and believe they would help streamline annual reports without diminishing the utility of the information provided to investors or weakening investor protections. We offer the following recommendations to clarify the proposals and increase the likelihood of the amendments achieving their desired results.

With respect to the first condition, we are concerned that it could be challenging to apply in practice, particularly in the year of implementation. For example, registrants could struggle to consistently evaluate whether discussion of the earliest of the three years is "material to an understanding of the registrant's financial condition, changes in financial condition and results of operations," particularly if they have traditionally provided two successive year-to-year comparisons. At a minimum, we suggest that the SEC revise the instruction to refer to "understanding of changes in the registrant's financial condition and trends in its results of operations." We believe this would promote a more appropriate consideration of the extent to which the earliest year is relevant to the discussion and analysis of the most recent year.

Also, it is unclear whether the first condition refers to discussion of the earliest of the three years in its entirety or whether the evaluation should consider selected aspects of that period, which we believe was the SEC's intent. Further, as discussed above, we are concerned about the use of the term "material" in the proposed amendment to the instructions. Therefore, we suggest that the instruction be

revised to allow the omission of discussion “about some or all of the information about the earliest of the three years that is not necessary to achieve the disclosure objectives of MD&A.” This would encourage registrants to take a “fresh look” at their MD&A every time it is filed, focus on disclosing multiyear trends and reduce repetition of previously filed year-to-year comparisons.

To this end, as part of its disclosure effectiveness initiative, we suggest that the SEC revise Item 303 of Regulation S-K to clearly identify its disclosure objectives, many of which are currently embedded within the instructions to Item 303 and were expressed in plain English in the Commission’s December 19, 2003, Interpretive Release. These objectives should be fundamental and broad enough to apply across industries and remain relevant over time, such as:

- ▶ Provide narrative explanation through the eyes of management necessary to understand financial condition, changes in financial condition and results of operations
- ▶ Provide the context in which the financial statements should be analyzed
- ▶ Discuss the quality and variability of earnings and cash flows, from operations and outside sources, and the likelihood that past performance will not be indicative of future performance based on known events and uncertainties

We believe such an approach would alleviate the challenges of applying the proposed amendment to the instructions to Item 303 that uses the term “material” in a narrower context than the total mix of information.

With respect to the second condition requiring discussion of the earliest of the three years in the registrant’s prior-year Form 10-K, if the objective is to make sure that investors have been provided with MD&A that makes direct comparisons to the earliest of the three years, it is unclear why consideration should be limited to the prior-year Form 10-K. Therefore, we suggest that the Commission expand the second condition to state “if such discussion was previously filed in any SEC filing on EDGAR by that registrant under the Securities Act of 1933 (Securities Act) or the Exchange Act of 1934 (Exchange Act), such as Form S-1, Form S-4, Form 10 and Form 8-K.”

Further, if the Commission expands the scope as we suggest in the paragraph above, the consequence would appear to be only to require two successive year-to-year comparisons (or an integrated discussion covering all three years) in an initial public offering (IPO) registration statement of an entity that presents three years of audited financial statements. As an alternative to a modified second condition, the amended instruction should be more explicit regarding the MD&A requirements in the IPO registration of an entity that presents three years of audited financial statements.

We support the Commission’s proposal to enact conforming changes to Item 5, *Operating and Financial Review and Prospects*, of Form 20-F to maintain a consistent approach to MD&A for domestic and foreign private issuers.

In our view, when an annual report includes the initial filing of retrospective revisions to prior-period financial statements, such as a retroactive adoption of a new accounting principle, correction of an error, realignment of reportable segments or reorganization of entities under common control, there

should be no requirement to update previously filed MD&A. Instead, in such a filing, the issuer would only need to consider a discussion of the earliest of the three years presented in the same manner as it would in any annual report. When retrospectively revised financial statements are initially filed in a registration statement, a Form 8-K or an amended annual report, we believe it would be appropriate to update MD&A most recently on file in many but not all cases, consistent with considerations for material changes today (i.e., Item 11 of Form S-3). The evaluation of whether to update MD&A should consider both the pervasiveness of the changes and their related financial statement impact. It would be helpful for the Commission to acknowledge that in its adopting release or, more preferably, in the instructions to Item 303.

Description of property

In our comment letter on the Concept Release for Regulation S-K, we recommended that the Commission eliminate Item 102, *Description of Property*, and incorporate disclosure objectives related to physical properties and all other critical resources (e.g., human capital, intellectual property, technology) in the broader discussion of the registrant's business. We continue to believe that Item 102 should be subsumed into the disclosure objectives of Item 101. The SEC's proposing release explained that a broader revision of Regulation S-K along these lines will be deferred to a later, more comprehensive project, which we support.

In the interim, we note that the proposed revisions to Item 102 include several references to "material" or "materiality" and with respect to that materiality evaluation, the proposed revision retains the related reference to Instruction 1 to Item 101. As discussed above, we recommend that references to these terms be avoided in the individual disclosure items in Regulation S-K. Instead, the disclosure objective for properties should be to identify assets that contribute significantly to enterprise value, that are unique or provide competitive advantage, that could not be readily replaced or that present a significant risk to the enterprise if the registrant loses their use or access to them.

Risk factors

We support the proposal to omit the examples of possible risk factor disclosures from the relocated Item 105, *Risk Factors*, and to require the use of plain English when disclosing risk factors. Consistent with our previous comment letters, we believe that risk factor disclosures could be more informative by describing the expected consequences to the registrant with more specificity, presenting the risk factors with the highest probability of occurrence or largest potential magnitude first, and incorporating insights from the company's risk management processes.²

Hyperlinks and cross-referencing

We support the Commission's proposal to encourage registrants to avoid repetitive disclosures and promote more concise and user-friendly disclosure documents by using hyperlinks and cross-references to content elsewhere in the same filing and to other filings on EDGAR.

² For example, our 21 July 2016 letter on the concept release on Regulation S-K

We recommend that the adopting release and amendments contain instructions on how registrants would make clear which hyperlinks and cross-references to content in other filings with the SEC are provided for reader convenience and navigability and which ones relate to information incorporated by reference in the current filing. We note that because auditors have to consider any information incorporated by reference to be “other information in a filing that contains audited financial statements,” it would be critical for registrants to make this distinction so the auditor could comply with both of the following requirements:

- ▶ Identify the other information in a filing, the related scope of his/her professional responsibility and what constitutes “a document,” as defined in PCAOB Auditing Standard (AS) 2710, *Other Information in Documents Containing Audited Financial Statements*
- ▶ Perform a reasonable investigation in conjunction with assuming Section 11 liability with respect to an effective registration statement that includes his/her audit report in accordance with PCAOB AS 4101, *Responsibilities Regarding Filings Under Federal Securities Statutes*.

The PCAOB’s most recent agenda includes a project on the auditor’s responsibility regarding other information.³ We encourage the SEC to closely monitor this project so that any resulting standard setting defines the scope of other information with sufficient clarity when hyperlinks and cross references are used.

Financial statements

We appreciate the Commission’s responsiveness to concerns expressed by us and other public accounting firms about the scope of the auditor’s report when the financial statements and notes thereto refer to content residing elsewhere. We agree with the proposed prohibition of cross-references in the financial statements to information disclosed outside the financial statements unless permitted by SEC rules.

While we support the proposal to prohibit cross-references in the financial statements, we understand that there are certain standards in IFRS (e.g., IFRS 7, *Financial instruments: Disclosures*) that permit certain disclosures that are part of the audited financial statements to be located outside the related notes with a cross-reference in the notes that identifies this information. We suggest that the SEC consider allowing cross-referencing when it is expressly permitted by the accounting standards applied by the registrant, such as IFRS, but require any information that has been cross-referenced in the financial statements to be clearly identified as an integral part of the audited financial statements.

We also support the proposal to amend Item 407(d)(3)(i)(B) to refer more broadly to the “applicable requirements of the PCAOB and the Commission’s rules,” since the reference to PCAOB interim standard AU 380 is indeed outdated.

³ PCAOB [Standard-Setting Update](#), 30 September 2017, pages 5 - 7.



Forms

To provide registrants with more flexibility in how they present their disclosures, the proposal would amend Forms 10, 10-K and 20-F to allow registrants to exclude numbers and captions specified in the respective forms (but not captions required expressly by the form or Regulation S-K) and instead create their own captions and order of presentation. We support the proposal to provide registrants more flexibility in organizing disclosures and tailoring their presentation. This is consistent with principles-based disclosure objectives and would help reduce repetition and the need for cross-references. To facilitate investor navigation, a registrant that does not follow the order of presentation prescribed by the periodic reporting form should be encouraged to provide a table showing where the disclosures required by the form can be found.

* * * * *

We would be pleased to discuss our comments with the Commission or its staff at your convenience.

Yours sincerely,

Copy to:

Mr. William Hinman, Director, Division of Corporation Finance
Mr. Kyle Moffatt, Acting Chief Accountant, Division of Corporation Finance
Mr. Wesley R. Bricker, Chief Accountant, Office of Chief Accountant

**Appendix – Materiality references in Regulation S-K
(excluding Items 1110-1122 and Subparts 1200 requiring disclosures by oil and gas registrants
and Subpart 1100 requiring disclosures for asset-backed securities)**

Materiality definition/context	Number of times It occurs in Regulation S-K	Item reference within Regulation S-K of each occurrence
Material features/factors/terms in contracts	44	305(a) Instruction B; 402(e)(1); 402(e)(1)(i); 402(e)(1)(ii); 402(e)(1)(iii); 402(h)(2) Instruction 4 (3); 402(h)(2) Instruction 4(3)(i); 402(i)(3); 402(i)(3); 402(i)(3)(iii); 402(j)(4); 402(j)(5); 402(k)(2)(vii) Instructions; 402(b)(2); 402(b)(2)(ix); 402(b)(2)(xiv) 402(n)(2)(iii) and (iv) Instruction 2; 402(o); 402(o)(1); 402(o)(4); 402(o)(5); 402(q); 402(q)(1); 402(q)(2); 402(r)(2)(vii) Instructions; 402(r)(3); 402(r)(3); 402(t)(3) Instruction; 402(t)(3)(iii) Instructions; 407(e)(3)(iii); 601 Instruction 2; 903(b); 903(b)(2); 910(b); 910(e)(3); 912(d)(1); 1001; 1001(1); 1004(a); 1005(e); 1006(c)(4); 1007(b); 1007(d)(1); 1009(a)
Material change	26	201 Instruction 2; 301 Instruction 4; 303(a)(1); 303(a)(2)(ii); 303(a)(3)(ii); 303(a) Instruction 8; 303(b); 305(a)(iii)(4); 402(k)(2)(iii) and (iv) Instructions; 402(n)(2)(v) and (n)(2)(vi) Instruction 2; 402(o)(2); 402(o)(2); 402(s)(5); 407(a)(2); 407(c)(3); 407(c)(3) Instruction 2; 407 Instruction 2; 512(a)(iii); 601(b)(3)(i); 701(f)(viii); 1124; 1125(k)(1); 907(c); 911(c)(3); 1006(c)(3); 1006(c)(5)
Material risk/risk exposure	13	305(a)(iii)(3); 305(b); 305(b) Instruction 1 B; 305(b) Instruction 1 B; 305(a) and 305(b) General Instruction 5 A; 305(a) and 305(b) General Instruction 5 A iii; 508(b); 902(b)(2); 903(b)(7); 904(a); 904(a)(2); 908(b)(3); 908(b)(2)
Material to results of operations/financial condition	13	302(a)(3); 303(a) Instruction 4; 303(a) Instruction 11; 303(b); 303(b)(1); 303(b)(1); 303(b)(2); 303(b)(2); 303(b) Instruction 3; 303(b) Instruction 3; 303(b) Instruction 4; 303(b) Instruction 5; 915(a)

Materiality definition/context	Number of times It occurs in Regulation S-K	Item reference within Regulation S-K of each occurrence
Material to compensation	11	402(b)(1); 402(b)(2)(ix); 402(b)(2)(xiv); 402(b) Instruction 1; 402(b) Instruction 3; 402(c)(2)(v) and (vi) Instruction 2; 402(d)(2)(viii); 402(d) Instruction 7; 402(o)(7); 402(r)(2)(vii); 402(u) Instruction 6
Material to the registrant	10	303(a)(1); 303(a)(4)(i)(d); 303(a)(4)(i)(d); 303(a)(4)(ii)(D); 402(s); 402(s); 506; 512(a)(6)(iii); 601(b)(10)(i); 201(a)(2)(iii)
Material transaction/event/item	10	304(b)(3); 401(f) Instructions; 402(o)(7); 508(c)(3); 601(b)(8); 905(d)(2); 907(a)(ii); 910(e)(2)(viii); 1005(b)(6); 1006(c)(2)
Material relationship	9	507; 202(b)(10); 508(a); 508(b); 508(i); 909(b)(v); 909(b)(v)(B); 911(a)(1)(iv); 1003(c)(2)
Material to investor or investment decision	9	303(a)(4)(i); 401(g); 401(g); 404(a)(6); 601(b)(2); 601(b)(8); 903(b)(1); 905(e); 910(d)
Material contract(s)	7	601(a)(4); 601(b)(2); 601(b)(10)(ii)(D); 601(b)(10)(iii)(A); 601(b)(10) Instruction 2; 1005(b); 1005(c)
Material estimates/assumptions	6	402(h)(2) Instruction 2; 402(j) Instruction 1; 402(t)(2) Instruction 3; 402(u) Instruction 4 5; 402(u) Instruction 4 5; 911(c)(4)(iii)
Materially different	6	503(d) Instruction 2 C; 505(a); 902(b)(3); 910(b)(2); 1004(a)(1)(x); 1004(a)(2)(v)
Material to information/material to understanding	5	303(a)(4) Instruction 2; 305(c); 401(e)(1); 402(b)(2); 914(a)
Materially limits	5	202(a)(4); 202(b)(8); 201(c)(1); 201(c)(1); 305(a)(iii)(2)
Accounting treatment, if material	4	1004(a)(1)(xi); 1004(a)(1)(xii); 1004(a)(2)(vi); 1004(a)(2)(vii)
Material conflict of interest	4	904(b)(ii); 905(b)(5); 909(a); 1005(d)
Material legal proceeding	4	103; 103 Instruction 3; 103 Instruction 4; 103 Instruction 5
Material uncertainties	4	301 Instruction 2; 303(a) Instruction 3; 305(a) and 305(b) General Instruction 5 A ii; 910(e)

Materiality definition/context	Number of times It occurs in Regulation S-K	Item reference within Regulation S-K of each occurrence
Material features/factors/terms	3	201(d)(3); 202(c)(5); 202 Instruction 4
Material interest to a related person	3	404(a); 404(a)(1)(b); 404(a)(6)
Material policies and procedures	3	404(b); 407(c)(ii); 905(d)(1)
Material portion of proceeds to a transaction	3	504 Instruction 3; 504 Instruction 4; 504 Instruction 5
Material to the registrant's business	3	303(b) Instruction 7; 601(b)(10)(ii)(B); 103 Instruction 5 A
Material to sales/revenue/income	3	303(a)(3)(i); 303(a)(3)(ii); 303(a)(3)(iii)
To the extent material	3	303(a)(4)Instruction 2 ; 305(a)(1); 1008(b)2
Material capital expenditures/resources/plans	2	303(a)(2)(i); 303(a)(2)(ii)
Material distribution/compensation to investor	2	902(b)(5); 905(b)(4)
Materially impacts fairness or reliability of financial statements	2	304(a)(1)(v)(C); 304(a)(1)(v)(D)
Materially relate to	2	911(a)(1); 911(1)
Material for prudent judgment	1	914 Instruction 1
Material to evaluation of	1	401(f)
Material underwriting discounts/commissions	1	404(d) Instruction 1
Materiality of derivative financial instruments	1	305(a) and 305(b) General Instruction 5 A i
Materially affect comparability	1	301 Instruction 2
Reasonably likely to become material	1	303(a)(4)(i)(c)
Grand total	225	