



Ernst & Young LLP
5 Times Square
New York, NY 10036

Tel: +1 212 773 3000
ey.com

Ms. Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

21 October 2019

Re: Request for Comment on Modernization of Regulation S-K Items 101, 103, and 105 (Release No. 33-10668; 34-86614; File No. S7-11-19)

Dear Ms. Countryman:

Ernst & Young LLP is pleased to provide comments to the Securities and Exchange Commission (SEC or Commission) on its proposal to amend Regulation S-K to modernize the disclosure requirements for the description of business, legal proceedings and risk factors.

We are highly supportive of the Commission's objective to improve disclosures for investors while simplifying compliance efforts for registrants. In particular, we support the proposed principles-based approach to certain disclosure requirements that would allow registrants to communicate more effectively to investors information that is more relevant, organized and focused on each registrant's facts and circumstances. We agree with SEC Chairman Jay Clayton's comment that "materiality should be the touchstone of our markets; and as our markets change, what may be material does change, which is why we need to have a principles-based approach to disclosure."¹

We note that the proposed amendments would incorporate several of our previous recommendations to the Commission,² and we believe the proposed changes would help achieve the Commission's objective.

However, we recommend that the Commission consider making the revisions described below to facilitate the implementation of the proposed amendments and the realization of their objectives.

Item 101 – description of business

General development of business

We believe the proposed elimination of a prescriptive five-year lookback period would give registrants the flexibility to focus on providing material information necessary for users to understand the development of their business. As a practical matter, it would be helpful for the rule to clarify that the objective is to elicit disclosures about recent developments in the business, not the company's corporate history from inception.

¹ [Testimony of the SEC before the U.S. House of Representatives Committee on Financial Services](#), 24 September 2019.

² Refer to [our comment letter](#) (2016 letter) on Concept Release on Business and Financial Disclosure Required by Regulation S-K (Release No. 33-10064; 34-77599; File No. S7-06016).

Under the proposal, the requirement for a “full discussion” of the general development of the business in a registrant’s initial registration statement would be retained. But in subsequent filings, the registrant could provide an update with a focus on material developments “in the reporting period,” while incorporating, by reference and providing a hyperlink to, the most recently filed disclosure that together with the update would present a full discussion of the general development of the business. The proposal states that “a reader would have access to a full discussion by reviewing the updated disclosure and one hyperlinked disclosure,” which would help focus investor attention on material developments in the reporting period.

While we support the proposal to amend Rule 101(a)(2), we believe there could be implementation challenges in using a single hyperlink to produce a “full discussion” because the term “reporting period” would appear to limit the period of time over which a registrant can provide an update about material developments. If the reporting period is meant to be limited to the most recent annual period, it would require a full discussion without a hyperlink at least biennially in annual reports, with the option to provide an update on material developments covering only the subsequent year in intervening annual reports. Alternatively, if the term “reporting period” is meant to cover all financial statement periods in the annual report, a cumulative update on material developments that is limited to two or three years would still require a full discussion without a hyperlink to be included in the annual report at least every three or four years, depending on whether the registrant is a smaller reporting company. If material developments could be provided on a cumulative basis over multiple years (i.e., beyond the financial statement periods in the annual report), issuers would less frequently need to file a full discussion without a hyperlink. If that was the Commission’s intent, the final rule should use a phrase such as “over the update period” instead of “in the reporting period.” To avoid any uncertainty, we recommend that the final rule clarify the acceptable method(s) of compliance in a manner that limits the frequency with which a registrant would need to file a full discussion without using a hyperlink.

We again encourage the SEC to consider alternative mechanisms for providing investors access to a full discussion of the general development of the business. In our 2016 letter, we recommended that the SEC adopt a company profile approach because we believe it would significantly improve the format and delivery of information to investors. Under this approach, a registrant would update the business section of its company profile with material developments at least annually so that the profile would always include the full discussion.

Narrative description of business

We support the proposal to provide a non-exhaustive list of disclosure topics in Item 101(c) for consideration for disclosure to the extent material. This would facilitate the disclosure of material information while providing registrants with the flexibility to tailor their disclosures.

Human capital disclosures

Chairman Clayton has said that “the historical approach of disclosing only the costs of compensation and benefits often is not enough to fully understand the value and impact of human capital on the performance and future prospects of an organization.”³ We believe human capital is one of a number of drivers of a company’s future prospects, and we encourage the SEC to foster a disclosure regime that balances the communication of short-term results with a perspective on long-term value creation.

³ [Remarks to the SEC Investor Advisory Committee](#). 28 March 2019.

Many companies have recently begun to voluntarily disclose information addressing long-term value,⁴ including human capital disclosures. Additionally, certain market participants^{5,6} have developed disclosure frameworks to facilitate relevant, reliable and comparable human capital disclosures. We encourage the SEC to continue monitoring the development of market-led approaches in this important area.⁷

The Commission has proposed to require, to the extent material to an understanding of the registrant's business, either taken as a whole or with respect to an identified segment, disclosure of a description of human capital resources, including any human capital measures or objectives that management focuses on in managing the business (such as, depending on the nature of the registrant's business and workforce, measures or objectives that address the attraction, development and retention of personnel). We believe this proposal should elicit more meaningful disclosures about human capital and its management. We note that a few of the Fortune 100 have begun to identify key performance indicators (KPIs) with respect to human capital, and some quantify actual KPI performance.

We also believe the SEC should encourage transparency and comparability of any quantitative disclosures companies choose to make about the human capital measures on which management focuses. To provide transparency, companies should disclose whether the measure conforms with a published framework or, if not, the basis of its computation. To promote comparability, companies could present or supplement human capital measures in proportion to inputs or outputs (e.g., measures per employee, full-time employee, salaried employee, unionized employee, hour worked, unit of production, store, revenue dollar). That is, a registrant could disclose that actual or planned performance was "30 hours of training per employee" instead of or in addition to "1 million training hours for the company."

Item 103 – legal proceedings

Environmental proceedings

Materiality should be the primary consideration in determining whether to make any disclosure. The Commission has proposed requiring disclosure of environmental proceedings to which the government is a party unless the registrant reasonably believes that the proceeding will result in monetary sanctions, exclusive of interest and costs, of less than \$300,000, up from \$100,000. We don't believe that the proposed increase of the bright-line threshold from \$100,000 to \$300,000 would determine materiality for registrants of all sizes and all industries. The proposal does not explain why such a threshold would be appropriate in driving material disclosures. Accordingly, we recommend that the Commission eliminate the proposed \$300,000 quantitative disclosure threshold and replace it with a materiality-based standard.

⁴ Refer to [our comment letter](#) on Earnings Releases and Quarterly Reports (Release No. 33-10588; 34-84842; File No. S7-26-18)

⁵ [Embankment Project for Inclusive Capitalism \(EPIC\) report on sustainable and inclusive growth, which was issued on 16 November 2018 and was co-created by the EY global organization.](#)

⁶ [Sustainability Accounting Standards Board \(SASB\)'s industry-specific sustainability accounting standards.](#) 7 November 2018.

⁷ SEC officials have said they are carefully monitoring the development of market-led approaches rather than regulatory ones in this area. Speech: [Applying a Principles-Based Approach to Disclosing Complex, Uncertain and Evolving Risks.](#) William Hinman, Director SEC Division of Corporation Finance. 15 March 2019.



Item 105 – risk factors

We commend the Commission for proposing amendments to address the significant volume of risk factor disclosures. We agree that a summary would help investors assess the risks that would affect their investment decisions. However, establishing a specific threshold of pages above which a summary would be required seems arbitrary, especially since similar disclosures presented in different formats can differ in length.

Instead of requiring a summary of risk factors only if the risk factors section exceeds 15 pages, we recommend that the SEC require all registrants to summarize their risk factors in the body of the filing. We believe that such summaries should enable readers to understand the overall risk profile, including material developments, by highlighting any new risk factors or those that might have changed materially since the last filing.

To further facilitate readability of the filing, we also recommend that the SEC allow registrants to present the complete discussion of risk factors separately from the body of the report (i.e., either in Part IV of the Form 10-K, as a filed exhibit, or incorporated by reference from the aforementioned company profile). This may balance certain costs and benefits noted in the proposal because a summary would help investors better understand the nature of risk factors and their relative significance when reading the report, while still providing ready access to filed disclosures sufficient to reduce potential litigation risks.

Transition

To give issuers enough time to plan for compliance, we recommend that the SEC provide guidance in the adopting release for any final rule on the timing of adoption and transition. For example, the SEC could require registrants to apply the guidance beginning with the fiscal year beginning after the effective date, with early adoption permitted.

* * * * *

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

Very truly yours,

Copy to:

Mr. William Hinman, Director, Division of Corporation Finance
Mr. Kyle Moffatt, Chief Accountant, Division of Corporation Finance