

# Client Alert

January 2020

## Upcoming Changes to 2020 Proxy Statements and Annual Reports

As our calendars turn to 2020, proxy and annual report season is upon us. The following provides an overview of some considerations to keep in mind as you get ready for this year's annual filings—specifically regarding 2019 updates to the disclosure requirements under Regulation S-K.

### Proxy Statements

- **Hedging Disclosure:** This 2020 proxy season marks the first in which most public companies will need to comply with the SEC's December 2018 rule requiring disclosure of hedging policies and practices for employees, officers and directors. Specifically, companies must disclose whether employees (including officers) or directors or their designees are permitted to purchase financial instruments or otherwise engage in transactions that hedge or offset any decrease in the market value of a company's equity securities granted to the employee or director as compensation or held directly or indirectly by the employee or director. See new Item 407(i) of Regulation S-K. This new hedging disclosure is in addition to the proxy statement disclosure requirement related to hedging policies affecting executive officers to the extent material to the discussion of such officers' compensation that most public companies currently include in the Compensation Discussion and Analysis (CD&A) section of their proxy statement. For various technical reasons, we suggest that companies include this new disclosure outside of the CD&A section of the proxy statement.

Companies generally must include this new information in proxy statements for the election of directors during fiscal years beginning on or after July 1, 2019 (other than "smaller reporting companies" and "emerging growth companies" that must comply beginning with proxy statements for the election of directors during fiscal years beginning on or after July 1, 2020).

- **Board Diversity:** In February 2019, the staff of the SEC's Division of Corporate Finance issued two identical compliance and disclosure interpretations (C&DI) related to Regulation S-K that address disclosure of a director's self-identified diversity characteristics. See [C&DI 116.11](#) and [C&DI 133.13](#). The new guidance states that to the extent a board or nominating committee, in determining whether to recommend an individual for board membership, has considered self-identified diversity characteristics of the director nominee (e.g., race, gender, ethnicity, religion, nationality, disability, sexual orientation or cultural background) and the individual has consented to the company's disclosure of those characteristics, then the company's proxy statement should include an identification of those characteristics and how they were considered. Similarly, the staff expects the description of a company's diversity policy to discuss how the company considers the self-identified diversity attributes of nominees, as well as any other qualifications its diversity policy takes into account (e.g., work experience, military service, socio-economic or demographic characteristics).
- **Heading for Section 16 Filing Disclosures:** The heading for disclosures of late Section 16 filings has been changed to "Delinquent Section 16(a) Reports" (instead of "Section 16(a) Beneficial Ownership Reporting Compliance"). If there are no delinquent Section 16(a) reports, Instruction 2

to Regulation S-K Item 405(a) specifically encourages companies to exclude this section all together.

- **Overboarding:** Companies should review the number of other public company boards their directors serve on and the overboarding policies of their largest institutional investors. Currently, ISS's policy is that a CEO should not sit on more than two outside boards plus his or her own company's board, while other directors (including non-CEO executives) can sit on up to five boards. Glass Lewis & Co.'s policy is that inside directors (i.e., CEOs and other NEOs) should not serve on more than two boards (including their own boards), while outside directors should be limited to five boards. Additionally, institutional investors are increasingly adopting their own overboarding policies, which sometimes deviate from ISS and Glass Lewis & Co. See our [client alert from November](#) regarding certain institutional investors' policies.

## Annual Reports

- **Cover Page:** The cover page of Form 10-K must include the trading symbol for each class of the company's listed securities (similar to the updated cover pages of Form 10-Q and Form 8-K). Additionally, the checkbox relating to late Section 16 filing disclosures should be removed. Also, as discussed in greater detail below, large accelerated filers must now (and other companies according to the specified phase-in periods) tag the cover page of Form 10-K (similar to their Forms 10-Q and Forms 8-K) in Inline XBRL format.
- **Management Discussion and Analysis (MD&A):** Revised Item 303(a) of Regulation S-K provides that a company may use any presentation for its MD&A that, in its judgment, enhances a reader's understanding of the company's financial condition, changes in financial condition and results of operations. Furthermore, when financial statements included in a filing cover three years, in certain circumstances, the updated instructions to Item 303(a) no longer require a discussion of the earliest year. Specifically, the discussion of the earliest year is not required if (i) discussion was already included in the company's prior filings on EDGAR and (ii) the company identifies the location in the prior filing where the omitted discussion may be found. Therefore, a year-end company will not need to discuss its fiscal 2017 results in its year-to-year comparison in its MD&A section of the upcoming Form 10-K; instead, it can simply refer readers to the applicable information in the prior year's Form 10-K.

Additionally, while companies must still include trend information in various sections of the MD&A (including liquidity and capital resources and results of operations), five-year selected financial data is no longer required to be discussed when trend information is important.

- **Critical Audit Matters:** Any critical audit matters (CAMs) or an affirmative statement that no such CAMs exist must be included in the audit reports for large accelerated filers for audits of fiscal years ending on or after June 30, 2019 (all other companies must comply for fiscal years ending on or after December 15, 2020). Any matter arising from the applicable audit that was communicated or required to be communicated to the audit committee will be a CAM if it: (i) related to accounts or disclosures that are material to the financial statements and (ii) involved an especially challenging, subjective or complex auditor judgment. We expect that most, if not all, companies will have at least one CAM in their upcoming audit reports. See SEC Release No. 34-81916.
- **Property:** Item 102 of Regulation S-K now requires disclosure of principal physical properties **only to the extent material** to the company. This should permit companies to reduce, or even eliminate, the list of physical properties included in their Form 10-K.
- **Hyperlinks:** Companies must provide hyperlinks to information that is incorporated by reference in their disclosures if that information is available on EDGAR, regardless of whether the information is in a document filed as an exhibit.

- **Exhibits:** Item 601(b)(4)(vi) of Regulation S-K now requires companies to provide an exhibit to Form 10-K containing a description of each class of securities that is registered under Section 12 of the Exchange Act. These new exhibits will take additional time to prepare; therefore, companies should build this into their internal timelines.
- **Inline XBRL:** Large accelerated filers that prepare their financial statements in accordance with US GAAP are required to use Inline XBRL for fiscal periods ending on or after June 15, 2019. Therefore, large accelerated filers with calendar end fiscal years will need to (i) use Inline XBRL formatting for their Forms 10-K, (ii) include the word “Inline” within the title description for any XBRL-related exhibits in the Exhibit Index and (iii) include a new Exhibit 104 related to the cover page interactive data at the end of the Exhibit Index. See Instruction 1 to paragraphs (b)(101)(i) and (ii) of Item 601 of Regulation S-K.

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