Public Chatter

In-House Perspectives: Disclosure Practices

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CONTENTS

In-House Perspectives: Disclosure Practices

Compiled by Broc Romanek, our in-house readers share tips, anecdotes, and thoughts about topics that arise in their daily practice.

A. Corp Fin Comments

1. "Organize your comment letter response by including the full text of the staff comment then inserting the company's response – followed by the next comment and your response. This creates a response letter that is easy to follow for the SEC Staff, your auditors and executives without having to flip between the Staff comment letter and your response.

Think about the intentions of the Staff comment and what the Staff may ask as a follow-up. In some situations, it may be wise to add additional information to close out the comment. Try to determine if the Staff comment can be answered by agreeing to include different/additional disclosure in future 10-Qs or 10-Ks and provide a sample of what the company intends to disclose. Some third parties will publish Staff comments from multiple issuers and identify hot topics.

Also, after a period of time, both the Staff comments and the issuer's responses are posted on Edgar with the issuer's other Edgar filings. Sometimes it helps to review these hot topics and comments – and responses from your peer companies – to help identify the purpose of the comment as well as acceptable responses.

If you really want a gold star from executives and your board, inform them of the hot topic comments from your peers and identify whether they apply to your company. In some cases, it may be a good idea to discuss these hot topic comments with your disclosure committee or board and tackle the issue in your disclosure before you receive a particular comment from the Staff."

2. "If you are replying to an SEC comment and you don't want the information public, make sure you comply with the SEC's rules and FOIA as needed."

3. "I actually like comment letters. The comment letter response process is a great way to build affinity between the lawyers, the CFO and the accountants. It's also a good opportunity to engage with Corp Fin and understand what they are looking for in your disclosures."

4. "Never fun, but no alternative but to deal with it. Read it. Read it again. Take a hard look at the specific disclosure that Corp Fin commented on. Was this a point about which you and colleagues struggled when writing that disclosure or is this comment a complete surprise? If the former, go back to your notes on that point. You may well have the start of your response to Corp Fin."

5. "You will need to manage communications within the company, with your auditor, and with the board about the Staff's comments (the Audit Committee will want to know about the comment letter and company response). Pull together your thoughts on for the response letter and potential responses to ensure that everyone is working off the same page. Be open to feedback and suggestions."

6. "I'm not one whose first reaction is to call outside counsel. But when you receive an SEC comment letter, your outside counsel can be a great source of information and advice. They have a dataset greater than one; they have lots of clients who also are receiving comment letters.

They can tell you if they're seeing the same comment going to their other clients – or if you're alone. They also have networks they can tap anonymously for an even broader sample. Outside counsel can sometimes make a call to Corp Fin to ask clarifying questions. All of these data points help you frame your response and future actions."

7. "When I worked on the Staff, writing comments while reviewing a filing was real fun. The kind of fun you run home to tell your kids about."

B. What Are "Best Practices," Anyway?

1. "To me, 'best practices' means doing (or trying to do) what's right and not the bare minimum permitted. A former colleague of mine used as her mantra, 'Show me the rule where that disclosure is specifically required.' I always found that a terrible way to conduct a governance practice. As with anything, there are nuances to putting best practices in place, but it should start from a place of wanting to do the right thing."

2. "I agree that 'best practices' seems to be all over the map. First, what is it? Is it uber-conservative advice? Doing something in an abundance of caution? Or is it really a platinum standard? I often don't know."

3. "I really prefer not to use the term 'best practices,' but unfortunately it is thrown around often. I like to think it means the best of practices, but then what would it mean in the governance space to fail to comply with 'best practices,' especially if you are trying to be at—or reach—the top rung of the ESG ladder?"

4. "At my company, we try to use the phrase 'best fit' rather than 'best practice.' Although 'most common practice' is acceptable too."

5. "I agree that 'best practices' for some companies may actually be staying in the 'middle of the lane'—particularly if the 'gold standard' isn't well accepted yet and may be subject to some further refinement. Good examples I can think of are those who were early adopters of pay ratio and pay-versus-performance (PVP) disclosure. But I can't think of anyone giving those companies credit for what may now be a noncompliant approach and they may have just created internal inefficiencies when they had to retool those processes."

6. "My first General Counsel hated the term 'best practices' and we knew better than to use the phrase around him. I think the term aroused the same feelings as those that all of us have felt when lawyers say, 'this is market' or 'that is not market.' That sort of terminology assumes that there is one market term for a deal despite the underlying dynamics and that there is one way of doing something that is always best regardless of the underlying corporate/industry/fill-in-the-blank dynamics."

7. "Generally, I really like seeing 'best practices' and use it as an opportunity to directionally get a sense of whether there is anything new, unique, or different I need to delve into. It seems like recently, however, there are a lot of repeat best practices in the same space so that's not all that helpful. Perhaps I'm just getting older, but sometimes those words are followed by a small dose of skepticism, including thoughts like, 'what angle is trying to be pushed here?'"

8. "I really don't like the term 'best practices,' particularly when it's used—as it frequently is—in the singular (i.e., best practice). One size does not fit all; in fact, it sometimes doesn't fit one. The most I'll offer is 'leading practices,' but even that has its pitfalls."

C. Disclosure Controls

1. "We have refreshed the design of our cybersecurity governance and internal/external reporting framework to take into account the heightened reporting requirements in the pending rules. We're not there yet on climate, though.

I was surprised how challenging some of the cybersecurity governance modifications were because cybersecurity has been a concern for quite some time and processes have been in place for at least a decade. It still requires work to ensure everything is accounted for in disclosure controls." "Keep your expectations realistic and accept up front that your team will miss a deadline, make a mistake and run into a time-crunch-induced schedule disruption. Once you let those worries go before the season starts, then focus on the big stuff – the things that have to be completely right and the deadlines that don't have any flexibility."

2. "The SEC's new climate rules feel like déjà vu. Like 2002 all over again when Sarbanes-Oxley put COSO on the map for the typical disclosure lawyer. I'm too old for this stuff."

3. "Data and systems to support the data to ensure we're receiving accurate information and that they have a reliable source is our biggest challenge in anticipating the SEC's climate rules and how they will impact disclosure controls. It's an interesting exercise as it makes you rethink a lot of your existing processes and how they might dovetail with all these new ones."

4. "The recent SEC action that resulted in a company paying $35 million to settle charges that it failed to maintain adequate disclosure controls is an eye-opener. That case was about a lack of controls to review employee complaints about workplace misconduct. It also concerned impeding former employees from talking to the SEC about possible securities law violations by using separation agreements that required those former employees to notify the company if a government agency contacted them.

That company had the fairly common risk factor about the ability to attract and retain employees in its SEC filings. And the company's failure to percolate information about the nature and volume of employee complaints to the company's disclosure committee so that the committee might modify the risk factor was deemed inadequate by the SEC's Enforcement Division. So did the notification clause in the separation agreement that departing employees signed, even though there were no instances of a former employee actually being told not to talk to the SEC. Scary stuff."

5. "The composition of disclosure committees can be tricky. Historically, the most consistent source of headaches has been organizational changes affecting directors and senior leadership that might have Item 5.02 disclosure consequences, or that might affect which individuals should be deemed an 'Officer.' HR organizations tend not to consider disclosure obligations when these topics first arise, and they tend to have a hyper-developed culture of confidentiality."

6. "We spent time aligning with our information security team on what makes a cyber incident sufficiently significant that it should be promptly discussed with a disclosure controls working group.

The objective was that the information security team would not be making decisions about whether an incident is "material" and would report the "significant" incidents quickly for disclosure consideration.

We also added to our disclosure working group a lawyer who supports our cybersecurity and privacy compliance efforts, for ongoing alignment on related disclosure objectives."

7. "I still blame Enron for too much emphasis on "check the box" practices, sometimes to the exclusion of a thoughtful analysis and discussion. There is now a full generation or more of people who rely on certifications as a substitute for doing the hard work of understanding the intricacies of a business and determining what should be disclosed in any given situation."

8. "Disclosure controls? Ugh. If I wanted to be an accountant, I would have become a CPA."

9. "We modified our disclosure controls about seven years ago over cybersecurity incident concerns. Any new rulemaking in that area will probably not cause us to do much in the way of change.

But the new SEC climate rules will have a sizable impact on our controls and we have been mapping that out in draft form for the past year. We recently added a lawyer to our disclosure working group who supports our climate change initiatives, to help with alignment on disclosure objectives."

10. "Ahead of the SEC's climate rules, our Controller's office has been leading the way by creating a mammoth spreadsheet in an effort to figure out where we may need to change our controls, both internal and disclosure. We have also talked to several technology providers about assisting in this process."

D. Climate Teamwork

1. "Given that the new climate rule proposal puts a significant amount of new "E"-related disclosure within the scope of disclosure and internal controls, the ESG team should now include internal audit, technical accounting/SEC reporting, legal, environmental, health & safety teams, external auditors and attestation shops and, to a much greater extent, the board and various committees that oversee ESG-related topics, risks and opportunities.

Thinking through a timeline from now until the proposed implementation dates of the SEC's climate proposal is a good idea. The timeline should include all relevant board/committee meetings, what should be included on the agendas for these meetings related to rule proposals, and the various management workstreams needed to be completed in order to provide helpful report-outs to the board/committees."

2. "Collaboration is great in theory. Much harder in practice. Just sayin'."

3. "As we are working on assessing our climate materiality in earnest, we are at the beginning of what promises to be a long ESG journey. We have a cross-functional team led by IR, PR and Legal.

I would recommend reaching deep into your company because there are a lot of folks who are passionate and informed about these areas. They want to be involved and want to lead change. Plus you have to have senior executive buy-in and support, which is sometimes challenging. So when your investors ask IR, it helps with connectivity back-up to the C-suite!"

4. "We are in the third year of integrating departments and their efforts towards climate and I continue to be surprised by the challenges that surface. It seems it's a never-ending process of putting out fires or being completely off-guard." "Be aware of your optionality. Not all "virtual" meetings are the same. There are strategic and reasons for proceeding on a "virtual-only" or "hybrid" basis. If your state law doesn't generally allow virtual meetings (or only allows hybrid or in-person – there is a good state law survey out there to check)."

5. "We are fortunate that senior management is completely committed to transitioning our business model. The surprising part has been the rest of the workforce. They can't seem to wrap their heads around how dire the circumstances are."

6. "We hired a Chief Sustainability Officer for the first time last year. Unfortunately, she doesn't have a Corporate America background and the transition has been rough. The practicalities and realities of corporate life escape her and working remotely hasn't helped because it's hard to grasp that reality when working from home."

7. "It's imperative for each member of your ESG team to fall in line with the strategy. Having a strong leader of the effort – supported by the C-Suite and with some sort of project manager experience – might be the single most important factor in whether a company can pull this off.

It's hard to develop signposts that achieve real goals that match what a company has pledged to accomplish." "If you have a shareholder proposal, make sure the holder has an opportunity to present and answer any questions during the virtual meeting. We generally have a phone line for our most frequent proponents and informed them of the phone line in advance. Finally, look for other ways to engage your holders."

E. Section 16 Compliance Reminders

1. "Use trading window communications — communicate with Section 16 officers and directors at the beginning of every open trading window (email works great for this). Consider including important reminders about Section 16 requirements, explaining the process for obtaining pre-approvals and the process for preparation, review and filing of Section 16 reports.

Be patient and proactive — even with the best compliance training and reminders, many Section 16 officers and directors will need to be walked through the specific obligations and requirements. The key is making sure they reach out as far in advance as possible."

2. "I've always given new directors and officers a Section 16 memo and checklist with onboarding. These were drafted long ago (15 years+) by a law firm, and I've updated them every few years as I've changed companies. I just used it with a new director this week.

Otherwise, once onboard, I have our Stock Admin team handle all of their filings and we stay in close contact with the broker, investment advisor, estate lawyer, etc. Can be painful if their estate is complex and they like complex instruments (GRATS!), but it helps ensure compliance."

3. "Ah, Section 16 – the area of the law that I have been so unsuccessful in avoiding since 1990. Whenever I get away from it, it manages to find me again."

4. "I have developed a training program that we give periodically to new Section 16 officers. The most valuable thing I impart, though, is to call me before you do anything. They may not remember the specific requirements, but if they can remember to call me, then most issues can be avoided or resolved."

5. "Have a trading policy that requires all insiders to pre-clear all transactions."

– Remind all insiders of the pre-clearance policy requirement when sending out quarterly earnings blackout alerts.

– Try to have company shares in a "Company Account" that you have access to like Shareworks, or a broker provided by company.

– Have Company Accounts locked to limit transactions that are not cleared yet by Legal.

– Have Company Accounts set up to provide you with duplicate trade confirmations once they are cleared. Shareholder proposals? Is this a trick question?"

6. "The corporate secretary should calendar at least an annual Section 16 compliance reminder.

– The secretary may want to consider adding a periodic Section 16 reminder/update as an agenda item for a board meeting.

– The secretary should be prepared to provide both a director on-boarding and a departure Section 16 compliance memo.

– The secretary should calendar an annual check of the status of each director and Section 16 officer's SEC filing codes.

– The secretary should carefully calendar and coordinate the necessary Section 16 SEC filings associated with the annual cycle for granting and vesting of equity grants.

– The secretary should be prepared to advise directors and Section 16 officers regarding the filing obligations associated with transactions related to estate planning.

– If the secretary is responsible for Section 16 SEC filings, particular care should be taken with respect to using the correct filing codes (e.g. the proper code for a transaction within a 401(k) plan) – an incorrect code can attract the unwanted attention of the Section 16 plaintiff's bar." "Becoming a believer that, although more costly in the short term, negotiating with the proponent with a no-action request on file is most effective. Prior to that time, there is little incentive for demands to be moderated, and once the deadline passes you are without leverage if you have no such request."

7. "I provide new directors and officers with a Section 16 memo describing their obligations, a copy of our insider trading policy, and a POA as a part of their onboarding materials. From there, we provide quarterly blackout memos to Section 16 officers (different from the memo sent to our other designated associates subject to the blackout period) that not only explains the blackout period, but also reiterates the need to seek prior authorization before trading.

We file Form 4s by POA (using information typically provided by brokers and HR), but request sign-off from the Section 16 director/officer before actually filing (which we get 95% of the time). The annual

D&O questionnaire is another opportunity to remind them that they are Section 16 officers and remind them of their obligations."

8. "Section 16 is a small group, so we are all over them. When they become a Section 16, it is important to sit down and educate them what Section 16 (and other things) mean as a Section 16 person. And there is a memo.

But perhaps the most important thing for Section 16 and Board members: pre-clearance. A periodic reminder on the incidents that can trip you up is not bad: family members and rouge investment managers who rebalance and forget they cannot buy/sell your stock."

9. "Whenever we onboard a new Section 16 officer or director, we review with them their compliance obligations. However, since we handle all Section 16 filings on their behalf and all are subject to pre-clearance procedures for any transactions in our stock, we haven't seen the need to send ongoing reminders to folks."

10. "For new Section 16 Officers, cover Section 16 risks and obligations when you do their 'Public Company Bootcamp' training. (Yes, you should be doing 'Public Company Bootcamp' training.)

Annually, remind Section 16 Officers that you are there to help. Before they or anyone in their household even thinks about doing anything with company securities, talk to you! And, remind them, albeit gently, that Section 16 risks and obligations are personal to them."

11. "I love Section 16 compliance. Compliance reminders provide an opportunity to crack the whip on other executives and directors. The Board should annually appoint Section 16 officers (and acknowledge that directors are also subject to Section 16).

Immediately following this Board action, a Section 16 compliance memo should be circulated to the Section 16 officers and directors. I like to add in any recent or significant SEC actions against Section 16 violators or relating to short swing profit liability to really get people to focus on the importance of compliance.

Lastly, and this could be a biggie, make sure that if your trading policy or Section 16 procedures requires any notice or proof of delivery or receipt, that you keep a record that the company has complied with such notice, delivery or receipt.

For example, if the Section 16 policy states that periodic trading or blackout windows will be announced, then the company needs to not only comply with such obligation, but keep records to prove compliance. At the end of the day, Section 16 compliance falls on the individual executives and directors – but those same individuals are relying on their trusted lawyers to protect them from themselves."

12. "All of our filings are handled by POA. We send an email the night before to the senior management team, PR and IR that we are filing Form 4s at market close the following day to reflect [whatever the event is] [and a list of officers]. Notify us if you would like a copy. To date, no one has taken us up on the offer."

13. "Include the reminder in the annual D&O questionnaire, and, if performed, any quarterly questionnaire bringdowns used to comply with Auditing Standard 18 (now AS 2410)."

14. "Section 16 has been sort of unkind to me."

15. "I have generally found reminders about Section 16 obligations helpful to bundle with periodic reminders regarding insider trading policies, given the overlap.

Insiders often have a good handle on classic Section 16 triggers but triggers driven by estate planning and similar matters are easier to overlook; in my experience, these periodic reminders are an easy way to address that and avoid surprises being reported in the D&O questionnaire at year-end."

F. Rule 10b5-1 Plans

1. "If you are in the unfortunate circumstance where an executive or director is terminally ill or having high-risk surgery, you should note that most 10b5-1 plans automatically terminate at death. This becomes particularly tricky if the plan covers stock options with an impending expiration date.

In our case, the broker permitted the individual to assign all obligations under an existing 10b5-1 plan to her family trust. Under the terms of the Assignment and Assumption Agreement (signed by the individual, the Trustee and the broker), sales under the plan could continue after death so long as the Trust remained in existence."

2. "At the risk of sounding a bit pedantic – or perhaps like I'm telling the SEC to get off my lawn – I'll weigh in on the reworking of Rule 10b5-1 that appears to be coming our way. Most of the parade of horribles described by SEC Chair Gensler as abuses of the Rule appear – to me at least – to be less about deficiencies within the Rule than about the fact that the insider didn't have a valid plan in the first instance.

Since a lack of MNPI is a prerequisite for having a valid plan, what exactly would be the point of mandating a cooling-off period? The insider either has no MNPI (in which case, a cooling-off period is superfluous) or has MNPI (in which case, they don't have a valid plan). Perhaps if the SEC spent a bit more time actually pursuing 10b-5 violations, we wouldn't need to hamstring the rest of the market with mandatory cooling-off periods or similar structures."

3. "I have always worked with the Company's brokers to make sure that the form of 10b5-1 plan comports with the Company's insider trading policy. At my current company, we strongly encourage our senior execs directors to enter into 10b5-1 plans if they want to trade. We review all of these plans against a pretty strict policy. We do our best to limit the number of brokers involved.

In a past life, we had one employee who entered into a very complicated plan. Not only did the sales wind up firing close to earnings, he also put himself at risk of not meeting executive holding requirements. My take-away: too complicated a plan is bad. (The algorithms that the executive picks to figure out what to see is up to then.) But on the execution end, with Forms 4 and continued scrutiny, KISS.

Also, try to avoid sales that are scheduled to occur prior to the earnings calls. Even though they are 10b5-1 sales (and we require those to be disclosed on every relevant Form 4), not everyone reads the footnotes."

4. "Before I sign a 10b5-1 Plan, I send this message to the insider: 'Can you please confirm that you are not in possession of material, non-public information? The materiality of information depends upon the circumstances. Information is considered "material" if there is a substantial likelihood that a reasonable investor would consider it important in making an investment decision, or if the facts would have been viewed by the reasonable investor as having significantly altered the "total mix" of information publicly available. Material information can be positive or negative and can relate to virtually any aspect of a company's business and impact the value of any type of security – debt or equity.' This is pursuant to our Company Insider Trading Policy.

Under the Insider Trading Policy, as amended, once you have a 10b5-1 plan in place, I cannot approve (i) modifications to or cancellations of the plan, (ii) trades outside of the plan or (iii) any additional plans (only one plan operating at a time). Please make sure the plan captures your trading needs for its duration."

5. "Regarding 10b5-1plans, I recommend that a company's securities/insider trading policy require pre-approval of all 10b5-1 plans adopted by anyone subject to the policy."

6. "Ugh. I can't stomach these."

7. "Our Insider Trading Policy includes an addendum specifically devoted to 10b5-1 Plans (rules, requirements, cooling off period, review process, etc.) The Trading Plan document must be reviewed and counter-signed by the legal team. For Section 16 officers – despite the obvious purpose of entering into a plan – a plan may not permit trading within 10 days before earnings.

We don't like the optics of filing Form 4s around earnings. Insiders must have a pre-clearance interview with the legal team prior to entering into a plan. Following that pre-clearance interview, a confirmation email is sent to the individual and the broker."