

LEGAL ALERT

Securities Law and Practice Updates

December 2020

Revisions to the SEC MDA Rules

I. SEC ADOPTS AMENDMENTS TO FINANCIAL DISCLOSURE RULES UNDER REGULATION SK

A. Overview of the Amendments

On November 19, 2020, the Securities and Exchange Commission ("SEC") adopted significant amendments to the financial disclosure rules under Regulation SK of the Securities Act of 1933, as amended (the "Securities Act"), which will:

- Eliminate Item 301(Selected Financial Data); and
- Modernize, simplify, and streamline Item 302(a) (Supplementary Financial Information) and Item 303(Management's Discussion). Specifically, these amendments will:
 - Revise Item 302(a) to replace the current requirement for quarterly tabular disclosure of specified operating results with a principles-based requirement for disclosure about material retrospective changes in such results;

We are able to provide counsel and guidance in SEC and New Mining Disclosure matters. For additional information, please contact the attorneys named below or the attorney with whom you have a primary relationship.

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- Add a new Item 303(a), Objective, to state the principal objectives of MD&A;
- Amend Item 303(a), Full fiscal years (amended Item 303(b)) and Item 303(b), Interim periods (amended Item 303(c)) to modernize, clarify, and streamline the items;
- Replace Item 303(a)(4), Off-balance sheet arrangements, with an instruction to discuss such obligations in the broader context of MD&A;
- Eliminate Item 303(a)(5), Tabular disclosure of contractual obligations, and amend Item 303(b)(1), Liquidity and Capital Resources, to specifically require disclosure of material cash requirements from known contractual and other obligations as part of an enhanced liquidity and capital resources discussion; and
- Add a new Item 303(b)(3), Critical accounting estimates, to clarify and codify SEC guidance on critical accounting estimates.

The SEC also adopted certain parallel amendments to Forms 20-F and 40-F, including Item 3.A of Form 20-F (Selected Financial Data), Item 5 of Form 20-F (Operating and Financial Review and Prospects), General Instruction B.(11) of Form 40-F (Off-Balance Sheet Arrangements), and General Instruction B.(12) of Form 40-F (Tabular Disclosure of Contractual Obligations).

The amendments will be effective thirty days after the Adopting Release has been published in the Federal Register. Registrants will be required to apply the amended rules for their first fiscal year ending on or after the date which is 210 days after the Adopting Release is published in the Federal Register (the "mandatory compliance date"). Registrants will be required to apply the amended rules in a registration statement and prospectus that on its initial filing date is required to contain financial statements for a period on or after the mandatory compliance date. Although registrants will not be required to apply the amended rules until their mandatory compliance date, they may provide disclosure consistent with the final amendments any time after the effective date, so long as they provide disclosure responsive to an amended item in its entirety.

II. DESCRIPTION OF THE AMENDMENTS

A. Selected Financial Data (Item 301)

Current Item 301 requires registrants to furnish selected financial data in comparative tabular form for each of the registrant's last five fiscal years and any additional fiscal years necessary to keep the information from being misleading. The amendments eliminate Item 301.

B. Supplementary Financial Information (Item 302)

Current Item 302(a)(1) requires disclosure of selected quarterly financial data of specified operating results, and current Item 302(a)(2) requires disclosure of variances in these results from amounts previously reported on a Form 10-Q. Item 302(a) does not apply to smaller reporting companies ("SRCs") or foreign private issuers ("FPIs") and, because it only applies to companies that already have a class of securities registered under Section 12 of the Securities Exchange Act of 1934, as amended (the "Exchange Act") at the time of filing, it does not apply to first-time registrants conducting an initial public offering ("IPO") and registrants that are only required to file reports pursuant to Section 15(d) of the Exchange Act.

The amendments to Item 302(a) streamline its requirements to require disclosure only when there are one or more retrospective changes that pertain to the statements of comprehensive income for any of the quarters within the two most recent fiscal years and any subsequent interim period for which financial statements are included or required to be included by Article 3 of Regulation S-X and that, individually or in the aggregate, are material.

The amendments require registrants to provide an explanation of the reasons for such material changes and to disclose, for each affected quarterly period and the fourth quarter in the affected year, summarized financial information related to the statements of comprehensive income (as specified in Rule 1-02(bb)(ii) of Regulation S-X) and earnings per share reflecting such changes. The affected quarters may include, depending on the facts and circumstances, a single quarter in which the material retrospective change applies, or it may flow through to subsequent quarters during the relevant look-back period (i.e., the quarters within the two most recent fiscal years and any subsequent interim period for which financial statements are included or required to be included by Article 3 of Regulation S-X).

In a change from current Item 302(a), amended Item 302(a) will apply beginning with the first filing on Form 10-K after the registrant's initial registration of securities under sections 12(b) or 12(g) of the Exchange Act.

C. Management's Discussion and Analysis of Financial Condition and Results of Operations (Item 303)

Item 303 of Regulation S-K requires disclosure of information relevant to assessing a registrant's financial condition, changes in financial condition, and results of operations. The disclosure requirements for full fiscal years in Item 303(a) include five components: liquidity, capital resources, results of operations, off-balance sheet arrangements, and contractual obligations. Item 303(b) covers interim period disclosures and requires registrants to discuss material changes in the items listed in Item 303(a), other than the impact of inflation and

changing prices on operations. Item 303(c) acknowledges the application of a statutory safe harbor for forward-looking information provided in off-balance sheet arrangements and contractual obligations disclosures. Item 303(d) provides certain accommodations for SRCs.

Amended Item 303 of Regulation S-K includes the following principle changes:

- New Item 303(a) states the objectives of MD&A that will apply throughout amended Item 303. It also incorporates much of the substance of Instructions 1, 2, and 3 to current Item 303(a).
- Amended Item 303(b) provides the requirements for full fiscal year disclosure and comprises three main requirements:
 - Item 303(b)(1) provides the overarching requirements for liquidity and capital resources disclosures, and reflects an enhanced principles-based requirement focused on material short- and long-term cash requirements, including those from known contractual and other obligations. Items 303(b)(1)(i) and (ii) provide the specific disclosure requirements for liquidity and capital resources, respectively.
 - Item 303(b)(2) provides the requirements for results of operations disclosures, and includes minor amendments such as eliminating the current requirement to discuss the impact of inflation and changing prices where material; and
 - Item 303(b)(3), requires disclosure of critical accounting estimates, and largely clarifies and codifies SEC's guidance in this area.
- Amended Item 303(c) provides for interim disclosure requirements, and will allow for more flexibility in the interim periods compared. The item's instructions have also been streamlined by eliminating certain instructions and providing cross-references to similar instructions to Item 303(b); and

1. Restructuring and Streamlining

a. Objective of MD&A (new Item 303(a))

Amended Item 303(a) calls for the following disclosure:

- Material information relevant to an assessment of the financial condition and results of operations of the registrant, including an evaluation of the amounts and certainty of cash flows from operations and from outside sources.

- Material events and uncertainties known to management that are reasonably likely to cause reported financial information not to be indicative of future operating results or of future financial condition. This includes descriptions and amounts of matters that have had a material impact on reported operations as well as matters that are reasonably likely based on management's assessment to have a material impact on future operations.
- The material financial and statistical data that the registrant believes will enhance a reader's understanding of the registrant's financial condition, cash flows and other changes in financial condition, and results of operations.

b. Reasons underlying material changes (Amended Item 303(b))

The amendments have re-captioned current Item 303(a) as Item 303(b), which continues to apply to all MD&A disclosures. The amendments also moved to the amended Item 303(b) the portion of current Instruction 4 that provides that where the consolidated financial statements reveal material changes from year to year in one or more line items, the causes for the changes shall be described. The SEC also amended that portion of current Instruction 4 to clarify that MD&A requires a narrative discussion of the "reasons underlying" material changes rather than only the "causes" for material changes. The SEC also amended the item to clarify that registrants should discuss material changes within a line item even when such material changes offset each other.

c. "Segment information...other subdivisions (e.g., geographic areas product lines)" (Amended Item 303(b))

Item 303(a) currently requires that, where in the registrant's judgment a discussion of segment information and/or other subdivisions (e.g., geographic areas) of the registrant's business would be appropriate to an understanding of such business, the discussion shall focus on each relevant "reportable" segment and/or other subdivision.

The amendments include "product lines" as an example of a subdivision of a registrant's business that should be discussed where, in the registrant's judgment, it is necessary to an understanding of the registrant's business. This additional example is not intended to require product line disclosure where, in the registrant's judgment, it is not necessary to an understanding of the registrant's business. Rather, it is intended to remind registrants of the type of disclosure that may be required.

2. Capital Resources – Material Cash Requirements (New Item 303(b)(1) and Amended Item 303(b)(1)(ii))

Current Item 303(a)(2) requires a registrant to discuss its material commitments for capital expenditures as of the end of the latest fiscal period, and to indicate the general purpose of and the anticipated sources of funds needed to fulfill such commitments. A registrant also must discuss, among other things, any known material trends, favorable or unfavorable, in its capital resources, and indicate any expected material changes in the mix and relative cost of such resources.

The SEC has amended Item 303(a)(2) to specify that a registrant should broadly disclose material cash commitments, including but not limited to capital expenditures. Specifically, the amendments require a registrant to describe its material cash “requirements,” including commitments for capital expenditures, as of the end of the latest fiscal period, the anticipated source of funds needed to satisfy such cash requirements, and the general purpose of such requirements.

3. Results of Operations – Known Trends or Uncertainties (Amended Item 303(b)(2)(ii))

Item 303(a)(3)(ii) currently requires a registrant to describe any known trends or uncertainties that have had or that the registrant reasonably expects will have a material impact (favorable or unfavorable) on net sales or revenues or income from continuing operations. In addition, if the registrant knows of events that will cause a material change in the relationship between costs and revenues, the change in the relationship must be disclosed.

The SEC has amended Item 303(a)(3)(ii) to provide that when a registrant knows of events that are reasonably likely to cause (as opposed to will cause) a material change in the relationship between costs and revenues, such as known or reasonably likely future increases in costs of labor or materials or price increases or inventory adjustments, the reasonably likely change must be disclosed.

The amendments clarify that the “reasonably likely” threshold applies throughout Item 303, and that whether a matter is “reasonably likely” to have a material impact on future operations is based on “management’s assessment.”

The SEC’s Adopting Release for the amendments states that when applying the “reasonably likely” threshold, registrants should consider whether a known trend, demand, commitment, event, or uncertainty is likely to come to fruition. If such known trend, demand, commitment, event or uncertainty would reasonably be likely to have a material effect on the registrant’s future results or financial condition, disclosure is required. Known trends, demands,

commitments, events, or uncertainties that are not remote or where management cannot make an assessment as to the likelihood that they will come to fruition, and that would be reasonably likely to have a material effect on the registrant's future results or financial condition, were they to come to fruition, should be disclosed if a reasonable investor would consider omission of the information as significantly altering the mix of information made available in the registrant's disclosures. This analysis should be made objectively and with a view to providing investors with a clearer understanding of the potential material consequences of such known forward-looking events or uncertainties.

4. Results of Operations – Net Sales and Revenues (Amended Item 303(b)(2)(iii))

Item 303(a)(3)(iii) currently specifies that, to the extent the "financial statements" disclose "material increases" in net sales or revenues, a registrant must provide a narrative discussion of the extent to which such "increases" are attributable to increases in prices, or to increases in the volume or amount of goods or services being sold, or to the introduction of new products or services. The SEC previously clarified that a results of operations discussion should describe not only increases but also decreases in net sales or revenues. Accordingly, the amendments to Item 303(a)(3)(iii) clarify that the disclosure requirement applies to "material changes" in net sales or revenues, rather than solely to "material increases" in these line items.

5. Results of Operations – Inflation and Price Changes (Current Item 303(a)(3)(iv), and Current Instructions 8 and 9 to Item 303(a))

Item 303(a)(3)(iv) generally requires registrants, either for the three most recent fiscal years or for those fiscal years in which the registrant has been engaged in business, whichever period is shorter, to discuss the impact of inflation and price changes on their net sales, revenue, and income from continuing operations. Instruction 8 to Item 303(a) clarifies that a registrant is only required to provide this disclosure to the extent material. The instruction further states that the discussion may be made in whatever manner appears appropriate under the circumstances and that no specific numerical financial data is required, except as required by Rule 3-20(c) of Regulation S-X, which applies to FPIs. Instruction 9 to Item 303(a) states that registrants that elect to disclose supplementary information on the effects of changing prices may combine such disclosures with the Item 303(a) discussion and analysis or provide it separately (with an appropriate cross-reference).

The amendments eliminate Item 303(a)(3)(iv) and Instructions 8 and 9 to Item 303(a). However, under amended Item 303, registrants will be required to discuss the impact of inflation or changing prices if they are part of a known trend or uncertainty that had, or is

reasonably likely to have a material impact on net sales, revenue, or income from continuing operations. Further, amended Item 303 requires that, where the financial statements reveal material changes from period-to-period in one or more line items, registrants must describe the underlying reasons for these material changes in quantitative and qualitative terms, which may also implicate a discussion of inflation and changing prices.

6. Off-Balance Sheet Arrangements (New Instruction 8 to Item 303(b))

In 2002, the Sarbanes-Oxley Act was enacted and added Section 13(j) to the Exchange Act, which required the SEC to adopt rules providing that each annual and quarterly financial report required to be filed with the SEC disclose all material off-balance sheet arrangements. To implement Section 13(j), in 2003, the SEC adopted specific disclosure requirements for off-balance sheet arrangements in current Item 303(a)(4).

The amendments replace the current more prescriptive off-balance sheet arrangement definition and related disclosure requirement in Item 303(a)(4) with a new principles-based Instruction to Item 303(b). This instruction requires 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, changes in financial condition, revenues or expenses, results of operations, liquidity, cash requirements, or capital resources.

7. Contractual Obligations Table (Current Item 303(a)(5)) and Amended Item 303(b)(1) - Liquidity and Capital Resources

Under Item 303(a)(5), registrants other than SRCs must disclose in tabular format their known contractual obligations. The item requires a registrant to arrange its table to disclose contracts by type of obligations, the overall payments due, and by four prescribed periods.

The amendments eliminate Item 303(a)(5), but revise Item 303(b) to specifically require disclosure of material cash requirements from known contractual and other obligations as part of a liquidity and capital resources discussion.

The amendments to Item 303(b) are intended to clarify the requirements while continuing to emphasize a principles-based approach focused on material short- and long-term liquidity and capital resources needs, while also specifying that material cash requirements from known contractual and other obligations should be considered as part of these disclosures.

Specifically, these amendments:

- Create a new Item 303(b)(1) to provide the overarching requirements for liquidity and capital resources disclosures in order to clarify these requirements;

- Incorporate in Item 303(b)(1) portions of current Instruction 5 to Item 303(a), which defines “liquidity” as the ability to generate adequate amounts of cash to meet the needs for cash, clarifying its applicability to the liquidity and capital resources requirements more generally;
- Codify prior SEC guidance that specifies that short-term liquidity and capital resources covers cash needs up to 12 months into the future while long-term liquidity and capital resources covers items beyond 12 months;
- Require the discussion on both a short-term and long-term basis;
- Require the discussion to analyze material cash requirements from known contractual and other obligations and such disclosures to specify the type of obligation and the relevant time period for the related cash requirements;
- Include a new instruction that states that the discussion of material cash requirements from known contractual obligations may include, for example, lease obligations, purchase obligations, or other liabilities reflected on the registrant’s balance sheet; and
- Include a new instruction that states, consistent with prior SEC guidance, the analysis for all of Item 303(b) should be in a format that facilitates easy understanding and does not duplicate disclosure already provided in the filing.

8. Critical Accounting Estimates (New Item 303(b)(3))

While not specified in Item 303, the SEC has stated that when preparing MD&A disclosure, companies should consider whether they have made accounting estimates or assumptions where the nature of the estimates or assumptions is material due to the levels of subjectivity and judgment necessary to account for highly uncertain matters or the susceptibility of such matters to change; and the impact of the estimates and assumptions on financial condition or operating performance is material.

The SEC has amended Item 303 to add new Item 303(b)(4), which explicitly requires disclosure of critical accounting estimates, which are defined as those estimates made in accordance with generally accepted accounting principles that involve a significant level of estimation uncertainty and have had or are reasonably likely to have a material impact on the registrant’s financial condition or results of operations. For each critical accounting estimate, the amendments require registrants to disclose, to the extent material, why the estimate is subject to uncertainty, how much each estimate has changed during the relevant period, and the sensitivity of the reported amounts to the methods, assumptions, and estimates underlying the estimate’s calculation. The discussion on how much each estimate has changed may also be met through a discussion of changes in the assumptions during the

period. Lastly, the amendments provide that the discussion should provide quantitative as well as qualitative information when quantitative information is reasonably available and will provide material information to investors.

New Item 303(b)(3) will require registrants to disclose how much an estimate and/or assumption has changed over a relevant period. This is intended to allow an investor to better evaluate the uncertainty associated with the critical accounting estimate by observing changes in estimates or assumptions over time.

In addition, as required by current Item 303(b), new Item 303(c) will continue to require that MD&A disclosure for interim periods include a discussion of the material changes in items specified in the full fiscal year requirements in amended Item 303(b). As this applies to critical accounting estimates disclosure in discussion of interim periods, registrants would be required to discuss material changes to the full fiscal year disclosures.

9. Interim Period Discussion (Amended Item 303(c))

Current Item 303(b) requires registrants to provide MD&A disclosure for interim periods that enables market participants to assess material changes in financial condition and results of operations between certain specified periods. Current Item 303(b)(1) requires registrants to discuss any material change in financial condition from the end of the preceding fiscal year to the date of the most recent interim balance sheet. Current Item 303(b)(2) requires registrants to discuss any material changes in their results of operations for the most recent fiscal year-to-date period presented in their income statement, along with a similar discussion of the corresponding year-to-date period of the preceding fiscal year. If a registrant is required or elects to provide an income statement for the most recent fiscal quarter, the discussion must also cover material changes with respect to that fiscal quarter and the corresponding fiscal quarter in the preceding fiscal year. Current Item 303(b)(2) also states that registrants subject to Rule 3-03(b) of Regulation S-X providing statements of comprehensive income for the twelve-month period ended as of the date of the most recent interim balance sheet must discuss material changes of that twelve-month period as compared to the preceding fiscal year rather than the preceding period.

The SEC has amended current Item 303(b) (to be renumbered as proposed Item 303(c)) to allow for flexibility in comparisons of interim periods and to simplify the item. Specifically, amendments permit registrants to compare their most recently completed quarter to either the corresponding quarter of the prior year (as is currently required) or the immediately preceding quarter. Under the amendments, if a registrant elects to discuss changes from the immediately preceding quarter, the registrant must provide summary financial information that is the subject of the discussion for that quarter or identify the prior EDGAR filing that presents such information so that a reader may have ready access to the prior quarter

financial information being discussed. In addition, under the amendments, if in a subsequent Form 10-Q, a registrant changes the comparison from the comparison presented in the immediately prior Form 10-Q, the registrant would be required to explain the reason for the change and present both comparisons in the filing where the change is announced.

Additionally, the amendments will:

- Eliminate the text that states that registrants need not provide a discussion of the impact of inflation and changing prices, consistent with the amendments described above; and
- Amend current Item 303(b)(2) (amended Item 303(c)(2)) material changes in results of operations—to break the requirements into two subsections:
 - Amended Item 303(c)(2)(i) will continue to require registrants to discuss any material changes in their results of operations between the most recent year-to-date interim period(s) and the corresponding period(s) of the preceding fiscal year for which statements of comprehensive income are provided; and
 - Amended Item 303(c)(2)(ii) will, as discussed above, require registrants to compare their most recently completed quarter to either the corresponding quarter of the prior year (as is currently required) or the immediately preceding quarter.

Additionally, amended Item 303(c) will continue to require that the interim discussion and analysis must include a discussion of the material changes in items specified in the full fiscal year requirements in amended Item 303(b).

The amendments also eliminate language requiring registrants subject to Rule 3-03(b) of Regulation S-X that elect to provide a statement of comprehensive income for the 12-month period ended as of the date of the most recent interim balance sheet to discuss material changes in that 12-month period with respect to the preceding fiscal year, rather than the corresponding preceding period.

10. Safe Harbor for Forward-Looking Information (Current Item 303(c))

Item 303(c) currently states that the safe harbors provided in Section 27A of the Securities Act and Section 21E of the Exchange Act (together, “statutory safe harbors”) apply to all forward-looking information provided in response to current Item 303(a)(4) (off-balance sheet arrangements) and current Item 303(a)(5) (tabular disclosure of contractual obligations), provided such disclosure is made by certain enumerated persons. For current

Item 303(a)(4), current Item 303(c) further states that the “meaningful cautionary statements” element of the statutory safe harbors is satisfied if a registrant satisfies all of current Item 303(a)(4)’s requirements. Because the amendments eliminate both Items 303(a)(4) and (5), they also eliminate current Item 303(c), which specifically and exclusively refers to those disclosure requirements. The safe harbors in Securities Act Rule 175 and Exchange Act Rule 3b-6 (the “regulatory safe harbors”), will continue to apply to forward-looking information in MD&A disclosure.

11. Smaller Reporting Companies (Current Item 303(d))

Current Item 303(d) states that an SRC may provide current Item 303(a)(3)(iv) information for the most recent two fiscal years if it provides financial information on net sales and revenues and income from continuing operations for only two years. Item 303(d) also states that an SRC is not required to provide the contractual obligations table specified in Item 303(a)(5). Because the amendments eliminate current Items 303(a)(3)(iv) and (a)(5), the amendments also eliminate current Item 303(d), which specifically and exclusively references these two disclosure requirements.

However, notwithstanding the elimination of current Item 303(a)(5), new Item 303(b) specifically requires disclosure of material cash requirements from known contractual and other obligations as part of a liquidity and capital resources discussion. SRCs are currently required to provide MD&A disclosure addressing liquidity and capital resources, and should continue to provide this disclosure under the amended requirements.

D. Application to Foreign Private Issuers

The SEC has adopted corresponding amendments that will apply to FPIs providing disclosure required by Form 20-F or Form 40-F. The SEC has also adopted amendments to current Instruction 11 to Item 303 as proposed, which specifically applies to FPIs that choose to file on domestic forms.

For further information concerning the amendments, see the SEC’s Adopting Release as follows: <https://www.sec.gov/rules/final/2020/33-10890.pdf>