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HOUSE OF REPRESENTATIVES
REPORT
113–642

# DISCLOSURE MODERNIZATION AND SIMPLIFICATION ACT OF 2014

DECEMBER 2, 2014.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. HENSARLING, from the Committee on Financial Services, submitted the following

# R E P O R T

[To accompany H.R. 4569]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 4569) to require the Securities and Exchange Commission to make certain improvements to form 10-K and regulation S-K, and for other purposes, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment is as follows:

Strike all after the enacting clause and insert the following:

**SECTION 1. SHORT TITLE.**

This Act may be cited as the "Disclosure Modernization and Simplification Act of 2014".

**SEC. 2. SUMMARY PAGE FOR FORM 10-K.**

Not later than the end of the 180-day period beginning on the date of the enactment of this Act, the Securities and Exchange Commission shall issue regulations to permit issuers to submit a summary page on form 10-K (17 C.F.R. 249.310), but only if each item on such summary page includes a cross-reference (by electronic link or otherwise) to the material contained in form 10-K to which such item relates.

**SEC. 3. IMPROVEMENT OF REGULATION S-K.**

Not later than the end of the 180-day period beginning on the date of the enactment of this Act, the Securities and Exchange Commission shall take all such actions to revise regulation S-K (17 C.F.R. 229.10 et seq.)—

(1) to further scale or eliminate requirements of regulation S-K, in order to reduce the burden on emerging growth companies, accelerated filers, smaller reporting companies, and other smaller issuers, while still providing all material information to investors;

(2) to eliminate provisions of regulation S-K, required for all issuers, that are duplicative, overlapping, outdated, or unnecessary; and

(3) for which the Commission determines that no further study under section 4 is necessary to determine the efficacy of such revisions to regulation S-K.

**SEC. 4. STUDY ON MODERNIZATION AND SIMPLIFICATION OF REGULATION S-K.**

(a) STUDY.—The Securities and Exchange Commission shall carry out a study of the requirements contained in regulation S-K (17 C.F.R. 229.10 et seq.). Such study shall—

(1) determine how best to modernize and simplify such requirements in a manner that reduces the costs and burdens on issuers while still providing all material information;

(2) emphasize a company by company approach that allows relevant and material information to be disseminated to investors without boilerplate language or static requirements while preserving completeness and comparability of information across registrants; and

(3) evaluate methods of information delivery and presentation and explore methods for discouraging repetition and the disclosure of immaterial information.

(b) CONSULTATION.—In conducting the study required under subsection (a), the Commission shall consult with the Investor Advisory Committee and the Advisory Committee on Small and Emerging Companies.

(c) REPORT.—Not later than the end of the 360-day period beginning on the date of enactment of this Act, the Commission shall issue a report to the Congress containing—

(1) all findings and determinations made in carrying out the study required under subsection (a);

(2) specific and detailed recommendations on modernizing and simplifying the requirements in regulation S-K in a manner that reduces the costs and burdens on companies while still providing all material information; and

(3) specific and detailed recommendations on ways to improve the readability and navigability of disclosure documents and to discourage repetition and the disclosure of immaterial information.

(d) RULEMAKING.—Not later than the end of the 360-day period beginning on the date that the report is issued to the Congress under subsection (c), the Commission shall issue a proposed rule to implement the recommendations of the report issued under subsection (c).

(e) RULE OF CONSTRUCTION.—Revisions made to regulation S-K by the Commission under section 3 shall not be construed as satisfying the rulemaking requirements under this section.

## PURPOSE AND SUMMARY

In 1976, the Supreme Court's decision in *TSC Industries, Inc. v. Northway, Inc.* held that an omitted fact is material under the Federal securities laws if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote his or her shares.[1] Securities and Exchange Commission (SEC) Chair White, current Commissioners Gallagher and Piwowar, and former Commissioner Paredes have expressed their belief that investors are currently experiencing "information overload" and that the SEC needs to revamp its disclosure system. Ever-increasing amounts of disclosure make it difficult for investors to digest the information they receive and discern which information is most relevant. H.R. 4569 would direct the SEC to simplify its disclosure regime for issuers and investors by permitting issuers to submit a summary page on Form 10-K with appropriate cross-references to the content of the report. The legislation would also direct the SEC to revise Regulation S-K (Reg. S-K) within 180 days of enactment of the Act to more appropriately scale disclosure rules for emerging growth companies and smaller issuers, as well as to eliminate other duplicative, outdated, or unnecessary Reg. S-K disclosure rules for all issuers. Reg. S-K states the requirements for the content of the non-financial statement portions of registra-

[1] *TSC Industries, Inc* v. *Northway, Inc.,* 426 U.S. 438 (1976).

tion statements filed under the Securities Act of 1933 and various filings under the Securities Exchange Act of 1934 (Exchange Act). In addition to these revisions, H.R. 4569 would direct the SEC to further study Reg. S-K and engage in rulemaking to implement additional reforms to simplify and modernize Reg. S-K disclosure rules within 360 days of enactment of the Act.

## BACKGROUND AND NEED FOR LEGISLATION

Congress enacted the Federal securities laws following the stock market crash of 1929 primarily to ensure that "[c]ompanies publicly offering securities for investment dollars . . . tell the public the truth about their businesses, the securities they are selling, and the risks involved in investing.[2] In addition to the basic disclosure requirements contained in the Securities Act and the Exchange Act, the SEC has exercised its rulemaking authority over time to impose additional disclosure requirements on companies when a stock is initially sold and then on a continuing and periodic basis. As SEC Commissioner Daniel Gallagher has stated, "The SEC is first and foremost a disclosure agency.[3]

### *SEC integrated disclosure system*

Prior to 1982, separate disclosure regimes applied to Securities Act registration statements and Exchange Act periodic reporting, which frequently resulted in overlapping and duplicative requirements. In 1977, the SEC's Advisory Committee on Corporate Disclosure issued a report recommending that the SEC adopt a single integrated disclosure system that would set forth all of the SEC's general disclosure rules and incorporate a single disclosure form. Shortly after this report was issued, the SEC adopted the first version of Reg. S-K which sets forth substantive disclosure requirements applicable to both public offerings and ongoing reporting requirements.

In 1982, the SEC adopted the integrated disclosure system "to revise or eliminate overlapping or unnecessary disclosure and dissemination requirements wherever possible, thereby reducing burdens on registrants while at the same time ensuring that securityholders, investors and the marketplace have been provided with meaningful non-duplicative information upon which to base investment decisions.[4] In adopting the integrated disclosure system, the SEC also expanded and reorganized Reg. S-K, making it the repository for the uniform, non-financial statement disclosures filed with the SEC under both the Securities Act and the Exchange Act. In addition to Reg. S-K, Regulation S-X (Reg S-X) provides guidance on the form and content of required financial statements and specifies the footnotes and schedules that should be included in or filed with the financial statements.[5]

The Federal securities laws require publicly traded companies to disclose information on an ongoing basis. For example, U.S. public

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[2] *See* "The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation," available at *http://www.sec.gov/about/whatwedo.shtml#.U8RbnkAoF-4.*

[3] Commissioner Daniel M. Gallagher, Remarks at the 2nd Annual Institute for Corporate Counsel, Dec. 5, 2013 ("Gallagher Corporate Counsel Remarks").

[4] SEC Report on Review of Disclosure Requirements in Regulation S-K, Dec. 2013, available at *http://www.sec.gov/news/studies/2013/reg-sk-disclosure-requirements-review.pdf.*

[5] *See id.*

companies must submit to the SEC annual reports on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K for a number of specified events and must comply with a variety of other disclosure requirements. The annual report on Form 10-K provides a comprehensive overview of the company's business and financial condition and includes audited financial statements. Although similarly named, the annual report on Form 10-K is distinct from the "annual report to shareholders," which a company must send to its shareholders when it holds an annual meeting to elect directors. Because the typical 10-K filed by an issuer with the SEC is hundreds of pages long, investors often find it difficult to derive the important information about the company. Permitting issuers to submit a summary page would enable companies to disclose pertinent information in a streamlined fashion to investors without the fear of being sued. This document would also enable investors to more easily access the most relevant information about a company.

H.R. 4569 builds on Section 108 of the Jumpstart Our Business Startups Act (JOBS Act) (P.L. 112–106), which directed the SEC to study Reg. S-K in order to simplify and modernize disclosure rules. The SEC completed this study and submitted its report to Congress in December 2013. The report includes recommendations for "potential next steps, including an outline of economic principles to consider and preliminary conclusions that can be drawn from the staff's review of the disclosure requirements.[6] The report fails, however, to include any substantive recommendations for reforming specific outdated, duplicative, unnecessary, or overly burdensome Reg. S-K disclosure requirements.

The SEC's outmoded corporate disclosure system diverts corporate resources toward regulatory compliance and away from innovation, growth, and job creation. Moreover, this antiquated disclosure regime leads to unnecessarily long, complicated, and often immaterial public company disclosures, resulting in investor confusion and potentially suboptimal investment decisions. As Chair White and her fellow Commissioners have recently recognized, the SEC's disclosure regime must be studied and revamped for the benefit of companies and investors.

In an October 2013 speech, titled, "The Path Forward on Disclosure," Chair White stated:

> Clearly, the topic of disclosure and a consideration of ways to make it better are perennial topics, as they should be. And, even though improvements have been made over the years, there is still more to consider and still, in my view, a lot more to do . . . . Although our study regarding Regulation S-K will only be the first step, it will set the stage for the dialogue and path forward toward a meaningful review of our disclosure requirements. . . . We must continuously consider whether information overload is occurring as rules proliferate and as we contemplate what should and should not be required to be disclosed going forward.[7]

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[6] *Id.*

[7] SEC Chair Mary Jo White, "The Path Forward on Disclosure," Remarks before the National Association of Corporate Directors—Leadership Conference 2013, October 13, 2013.

Similarly, in a January 2014 speech, SEC Commissioner Michael Piwowar cited information overload in calling for a "top-to-bottom review of the Commission's disclosure regime." [8] In a January 2014 speech, Commissioner Gallagher also pointed to the dangers of information overload and called for revamping the SEC's corporate disclosure system. He stated, "Investors often say that disclosure documents are lengthy, turgid, and internally repetitive. Today's mandated disclosure documents are no longer efficient mechanisms for clearly conveying material information to investors, particularly ordinary, individual investors—myself included. . . . The complexity of today's disclosure requirements give [sic] the Commission cause for self-examination." [9] Commissioner Gallagher, however, indicated his preference for taking immediate, discrete steps to revamp clearly outdated or unnecessary SEC disclosure requirements, "rather than risk spending years preparing an offensive so massive that it may never be launched."

H.R. 4569 will ensure that the SEC streamlines and simplifies disclosures, follows the Supreme Court's well-established definition of materiality, and restores management discretion in identifying the material matters that should be disclosed to shareholders in periodic SEC filings.

## HEARINGS

The Subcommittee on Capital Markets and Government Sponsored Enterprises held a hearing on a discussion draft of H.R. 4569 on April 9, 2014.

## COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on May 7, 2014, and again on May 22, 2014, and ordered H.R. 4569 to be reported favorably to the House by a recorded vote of 59 yeas to 0 nays (Record vote no. FC–62), a quorum being present.

## COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto.

1. A motion by Chairman Hensarling to report the bill, as amended, to the House with a favorable recommendation was agreed to by a record vote of 59 yeas and 0 nays (Record vote no. FC–62).

[8] Commissioner Michael S. Piwowar, "Advancing and Defending the SEC's Core Mission," Remarks before the U.S. Chamber of Commerce, Jan. 27, 2014 ("Piwowar Core Mission Remarks").

[9] Commissioner Daniel M. Gallagher, Remarks to the Forum for Corporate Directors, Jan. 24, 2014 ("Gallagher Corporate Directors Speech").

Record vote no. FC-62

| Representative | Yea | Nay | Present | Representative | Yea | Nay | Present |
|---|---|---|---|---|---|---|---|
| Mr. Hensarling | X | | | Ms. Waters | X | | |
| Mr. Bachus | X | | | Mrs. Maloney (NY) | X | | |
| Mr. King (NY) | X | | | Ms. Velázquez | X | | |
| Mr. Royce | X | | | Mr. Sherman | X | | |
| Mr. Lucas | X | | | Mr. Meeks | X | | |
| Mr. Gary G. Miller (CA) | | | | Mr. Capuano | X | | |
| Mrs. Capito | X | | | Mr. Hinojosa | X | | |
| Mr. Garrett | X | | | Mr. Clay | X | | |
| Mr. Neugebauer | X | | | Mrs. McCarthy (NY) | X | | |
| Mr. McHenry | X | | | Mr. Lynch | X | | |
| Mr. Campbell | X | | | Mr. David Scott (GA) | X | | |
| Mrs. Bachmann | X | | | Mr. Al Green (TX) | X | | |
| Mr. McCarthy (CA) | X | | | Mr. Cleaver | X | | |
| Mr. Pearce | X | | | Ms. Moore | X | | |
| Mr. Posey | X | | | Mr. Ellison | X | | |
| Mr. Fitzpatrick | X | | | Mr. Perlmutter | X | | |
| Mr. Westmoreland | | | | Mr. Himes | X | | |
| Mr. Luetkemeyer | X | | | Mr. Peters (MI) | X | | |
| Mr. Huizenga (MI) | X | | | Mr. Carney | X | | |
| Mr. Duffy | X | | | Ms. Sewell (AL) | X | | |
| Mr. Hurt | X | | | Mr. Foster | X | | |
| Mr. Stivers | X | | | Mr. Kildee | X | | |
| Mr. Fincher | X | | | Mr. Murphy (FL) | X | | |
| Mr. Stutzman | X | | | Mr. Delaney | X | | |
| Mr. Mulvaney | X | | | Ms. Sinema | X | | |
| Mr. Hultgren | X | | | Mrs. Beatty | X | | |
| Mr. Ross | X | | | Mr. Heck (WA) | X | | |
| Mr. Pittenger | X | | | Mr. Horsford | X | | |
| Mrs. Wagner | X | | | | | | |
| Mr. Barr | X | | | | | | |
| Mr. Cotton | X | | | | | | |
| Mr. Rothfus | X | | | | | | |
| Mr. Messer | X | | | | | | |

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee has held hearings and made findings that are reflected in this report.

PERFORMANCE GOALS AND OBJECTIVES

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee states that H.R. 4569 will improve the usefulness and efficiency of SEC filings.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House of Representatives, the Committee adopts as its own the estimate of new budget authority, entitlement authority, or tax expenditures or revenues contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

COMMITTEE COST ESTIMATE

The Committee adopts as its own the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

CONGRESSIONAL BUDGET OFFICE ESTIMATES

Pursuant to clause 3(c)(3) of rule XIII of the Rules of the House of Representatives, the following is the cost estimate provided by the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
*Washington, DC, August 1, 2014.*

Hon. JEB HENSARLING,
*Chairman, Committee on Financial Services,*
*House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 4569, the Disclosure Modernization and Simplification Act of 2014.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contacts are Michael Hirsch and Susan Willie.

Sincerely,

DOUGLAS W. ELMENDORF.

Enclosure.

*H.R. 4569—Disclosure Modernization and Simplification Act of 2014*

H.R. 4569 would require the Securities and Exchange Commission (SEC), within 180 days of enactment, to revise certain registration and disclosure requirements for securities issuers with an aim to reduce the burden on smaller companies and to remove any duplicative or unnecessary provisions. The SEC also would be re-

quired, within 360 days of enactment, to report to the Congress on ways to further simplify those regulations and, 360 days after that, to issue a proposed rule based on the findings of the report.

Based on information from the SEC, CBO estimates that implementing H.R. 4569 would cost about $1 million over the 2015–2019 period to comply with the reporting and rulemaking requirements under the bill. The SEC is currently studying and in the process of revising certain registration and disclosure requirements, so the costs of the initial rulemaking required under the bill would not be significant. Most of the costs would be incurred to issue the report and complete a second rulemaking process. Under current law the SEC is authorized to collect fees sufficient to offset its appropriation each year; therefore, we estimate that the net cost to the SEC would be negligible, assuming appropriation action consistent with that authority. Enacting H.R. 4569 would not affect direct spending or revenues; therefore, pay-as-you-go procedures do not apply.

H.R. 4569 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would not affect the budgets of state, local, or tribal governments.

Assuming that the SEC increases fees to offset the cost of the second rulemaking that would be required by the bill, H.R. 4569 would increase the cost of an existing mandate on private entities that are required to pay those fees. Based on information from the SEC, CBO estimates that the aggregate cost of the mandate would fall well below the annual threshold for private-sector mandates established in UMRA ($152 million in 2014, adjusted annually for inflation).

The CBO staff contacts for this estimate are Michael Hirsch and Susan Willie (for federal costs) and Matthew Denneny and Patrice Gordon (for the private-sector impact). The estimate was approved by Theresa Gullo, Deputy Assistant Director for Budget Analysis.

## FEDERAL MANDATES STATEMENT

The Committee adopts as its own the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates reform Act.

## ADVISORY COMMITTEE STATEMENT

No advisory committees within the meaning of section 5(b) of the Federal Advisory Committee Act were created by this legislation.

## APPLICABILITY TO LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of the section 102(b)(3) of the Congressional Accountability Act.

## EARMARK IDENTIFICATION

H.R. 4569 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9 of rule XXI.

DUPLICATION OF FEDERAL PROGRAMS

Pursuant to section 3(j) of H. Res. 5, 113th Cong. (2013), the Committee states that no provision of H.R. 4569 establishes or reauthorizes a program of the Federal Government known to be duplicative of another Federal program, a program that was included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111–139, or a program related to a program identified in the most recent Catalog of Federal Domestic Assistance.

DISCLOSURE OF DIRECTED RULEMAKING

Pursuant to section 3(k) of H. Res. 5, 113th Cong. (2013), the Committee states that H.R. 4569 requires the Securities and Exchange Commission (SEC) to issue regulations in accordance with the bill.

SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

*Section 1. Short Title*

This section states that the Act may be cited as the Disclosure Modernization and Simplification Act.

*Section 2. Summary page for Form 10-K*

This section requires the SEC to issue regulations to permit users to submit a summary page on form 10-K under certain conditions.

*Section 3. Improvement of Regulation S-K*

This section requires the SEC to revise Regulation S-K to reduce or eliminate burdensome requirements on emerging growth companies, accelerated filers, and smaller reporting companies, and other smaller issuers.

*Section 4. Study on modernization and simplification of Regulation S-K*

This section directs the SEC to carry out a study of the requirements contained in Regulation S-K to improve its efficiency, and to report its findings to Congress, along with recommendations on how to improve efficiency, within 360 days of enactment.

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