

The SEC Adopts Rule Amendments Affecting Human Capital Disclosures

- JOHN ELLERMAN AND MIKE KESNER

Introduction

On August 26, 2020 the Securities and Exchange Commission (SEC) took steps to modernize the disclosure requirements under Regulation S-K by adopting amendments to the reporting of the business, legal proceeding, and risk disclosure descriptions in public company filings. Regulation S-K is a prescribed regulation under the U.S. Securities Act of 1933 which sets forth various SEC reporting requirements for public companies. Generally, Regulation S-K deals with narrative disclosures whereas Regulation S-X deals with financial statements. The specific amendments to Regulation S-K pertain to Item 101 (description of business), Item 103 (legal proceedings), and Item 105 (risk factor disclosures). The amendments are the first actions taken by the SEC in more than 30 years to update and streamline Regulation S-K disclosure requirements.¹

The updating of the human capital disclosure requirements as set forth in Item 101(C)(1) has been one of the most widely anticipated changes based on increased investor interest. SEC Chairman Jay Clayton stated in the release, “I am particularly supportive of the increased focus on human capital disclosures, which for various industries and companies can be an important driver of long-term value.”¹

Amendment to Rule 101(C)(1)

The rule amendments promulgated by the SEC are principles-based as opposed to prescriptive, as the SEC wanted to provide registrants with the flexibility to tailor their disclosures to the unique circumstances of each company — all in an effort to modernize, simplify, and update public disclosures for the benefit of registrants as well as investors. The amendment to Item 101(C)(1) revises three areas for reporting human capital. The first area is the general description of the registrant company’s human capital resources. Item 101(C)(1) requires — to the extent such disclosure is material to an understanding of the registrant’s business taken as a whole — a description of the registrant’s human capital resources, including any human capital measures or objectives that the registrant focuses on in managing its business. The final amendments identify various human capital measures and objectives that address the attraction, development, and retention of personnel as non-exclusive examples of subjects that may be material to the company’s business and workforce. The SEC clarifies by stating that the human capital measures and objectives cited are to be considered “examples of potentially relevant subjects, not mandates.”²

PARTNERS

Aubrey Bout	Mike Kesner	Jaime Pludo
Chris Brindisi	Donald S. Kokoskie	Matt Quarles
John R. Ellerman	Brian Lane	Lane T. Ringlee
John D. England	Joe Mallin	Brian Scheiring
R. David Fitt	Jack Marsteller	John R. Sinkular
Patrick Haggerty	Richard Meisheid	Christine O. Skizas
Jeffrey W. Joyce	Sandra Pace	Bentham W. Stradley
Ira T. Kay	Steve Pakela	Jon Weinstein

The SEC Adopts Rule Amendments Affecting Human Capital Disclosures

- JOHN ELLERMAN AND MIKE KESNER

The second area of Item 101(C)(1) addressed by the amendment is the SEC’s decision to not formally define the term “human capital” for reporting and disclosure purposes. Although many organizations commented that they would prefer a definition of human capital in the reporting guidance, the SEC has decided that the term “human capital” may evolve over time and may be defined by different companies in ways that are industry-specific. The SEC further notes that “there are many definitions of human capital and that the concept ... is often tailored to the circumstances and objectives of individual companies.”²

The third area of Item 101(C)(1) in the amendment is the registrant company’s need to disclose the number of persons employed by the company. The SEC stated this disclosure requirement can provide important and useful information that is material to an understanding of the registrant company’s business. The SEC indicated the disclosure of the number of persons employed by the registrant can help investors assess the size and scale of a registrant’s operations as well as changes in the business over time. However, the SEC is not requiring disclosure of additional metrics regarding the number of persons employed, such as data regarding full-time versus part-time or turnover statistics; rather, the SEC has indicated that such additional disclosures would be inconsistent with the principles-based approach adopted with the new disclosure requirements.

Summary Comments

The SEC’s principles-based approach to human capital disclosure allows companies to determine the employee demographic information and human capital management policies it believes will allow investors to better understand the company and assess the strength of its human resources. We expect a number of companies that have been waiting for the final SEC rule will begin to expand their current disclosures, and many companies will provide relevant information to help investors better understand the most valuable asset not reported on company’s the balance sheet.

The amendments to Regulation S-K will be effective 30 days after publication in the Federal Register.

General questions about this Viewpoint can be directed to John Ellerman at john.ellerman@paygovernance.com or Mike Kesner at mike.kesner@paygovernance.com.

¹ “SEC Adopts Rule Amendments to Modernize Disclosures of Business, Legal Proceedings, and Risk Factors Under Regulation S-K.” The U.S. Securities and Exchange Commission. August 26, 2020. <https://www.sec.gov/news/press-release/2020-192>.

² “Modernization of Regulation S-K Items 101, 103, and 105.” The U.S. Securities and Exchange Commission. August 26, 2020. <https://www.sec.gov/rules/final/2020/33-10825.pdf>.