Business Roundtable

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July 21, 2016

The Honorable Brent J. Fields
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: File No. S7-06-16, Release Nos. 33-10064, 34-77599
Business and Financial Disclosure Required by Regulation S-K

Dear Secretary Fields:

This letter is submitted on behalf of Business Roundtable, an association of chief executive officers of leading U.S. companies. Our member companies produce $7 trillion in annual revenues and employ nearly 16 million employees worldwide. Business Roundtable companies comprise nearly one-fifth of the total value of the U.S. stock market and annually pay more than $222 billion in dividends to shareholders, generate more than $495 billion in sales for small and medium-sized businesses and invest $129 billion in research and development.

Business Roundtable appreciates the opportunity to comment on the Securities and Exchange Commission's (the Commission or SEC) concept release on modernizing certain business and financial disclosures in Regulation S-K (the Concept Release). Our members believe that informative, clear and usable disclosures are essential to thriving capital markets and place a high value on modernizing and improving disclosures in a manner that continues to provide material information to investors. We agree that a "step-back" look aimed at improving our disclosure regime is appropriate. We are concerned that immaterial line-item disclosures and duplicative disclosure requirements both burden companies and do not provide investors with information necessary to make informed decisions.

In addition, since the U.S. public capital markets are a primary source of investment income for many Americans (e.g., to save for retirement or to pay for a child's education), the burdens imposed on public companies by the current volume and complexity of disclosure requirements under Regulation S-K and other SEC rules lead to fewer companies going and staying public, which, in turn, negatively impacts the depth and quality of U.S. capital markets. Ultimately, investors will be harmed by having access to fewer investment options that offer a reasonable rate of return. Adding to the regulatory burden on public companies leads to less investor choice, slower economic growth and a less competitive economy.

Materiality Is the Time-Tested Cornerstone of Securities Disclosures

For the better part of a century, the concept of materiality has established the optimal amount and content of required disclosures.[1] Materiality remains the linchpin of public company disclosure because it sets an investor-focused standard for the appropriate information to be shared, is customized to the particular characteristics and circumstances of each registrant and naturally addresses current issues as they emerge. Focusing disclosure requirements on materiality ensures that investors receive decision-driving company information without having to sift through an "avalanche of trivial information."[2]

A focus on materiality has the added benefit of eliminating unnecessary compliance costs for registrants that are ultimately borne by the investing public. Over time, the breadth of periodic disclosures has increased, increasing the cost and complexity of producing the reports. Much of this increase in the volume of disclosures is attributable to line-item requirements that, depending on the issuer, may or may not contain material information. This increased expense reduces the investment returns of shareholders, often providing limited value to that very constituency. In addition, the cost of compliance is a disincentive for companies to enter the public markets and has contributed to some registrants' decisions to go private.[3, 4] Today, there are fewer than 4,500 publicly traded companies, down from over 6,000 in 2000.[5] Compliance costs can be curbed by eliminating immaterial and repetitive disclosure requirements wherever possible.

The flexibility and efficiency afforded by a principles-based materiality construct dictate that disclosure requirements should remain grounded on this foundation. Disclosure requirements should compel registrants to provide all material information and to eliminate as much immaterial information as possible. If a disclosure requirement does not contribute to the overall mix of material information available to shareholders or reduce the disclosure of immaterial information, it should be regarded with skepticism.

Reporting Quality Is Optimized by Including Only Material Information

The benefits of materiality-focused disclosures are well illustrated when placed in contrast with the implications of prescriptive disclosure requirements. As noted in the Concept Release, the

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[1] The concept of materiality appeared as early as the Securities Act of 1933, 15 U.S.C. § 77q(a) (2012) ("It shall be unlawful for any person in the offer or sale of any securities . . . to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading.").
[2] TSC Industries, Inc. v. Northway, Inc., 426 U.S. 438, 448 (1976).
[3] See Geoff Colvin, *Going Private: Take This Market and Shove It*, FORTUNE (2016), http://fortune.com/going-private/.
[4] See Alix Stuart, *The True Costs of Being Public: More Than You Think*, CFO (2011), http://ww2.cfo.com/credit-capital/2011/11/the-true-costs-of-being-public-more-than-you-think/.
[5] See Geoff Colvin, *Going Private: Take This Market and Shove It*, FORTUNE (2016), http://fortune.com/going-private/.

Commission's disclosure requirements can largely be categorized as principles-based or rules-based.[6] Principles-based requirements ask registrants to apply their judgment to disclose only information that is material, while rules-based or prescriptive requirements result in disclosure based on bright-line rules irrespective of materiality, sometimes referred to as line-item requirements.[7] Relying on materiality-based requirements offers a number of advantages over prescriptive rules.

Materiality helps filter unnecessary information out of disclosures, providing investors a clearer picture of a company's business and financial profile and performance. Congress, courts and the Commission have all long recognized the importance of eliminating unimportant information from disclosures. The Commission has noted that "unnecessary detail" and "uninformative disclosure" serve to obscure material information.[8] Chair White has similarly cautioned that "information overload" hinders rather than aids investors' decision-making.[9] The use of prescriptive requirements without a materiality threshold invites regulations that impose potentially costly and distracting disclosures unrelated to investment decisions and, in some cases, serve the purposes of only a limited group of investors with a specific agenda that may not serve the best interests of the corporation or its shareholders taken as a whole.

Materiality – by its very definition – counsels companies to submit only useful information, for which "there is a substantial likelihood that a reasonable shareholder would consider the information important"[10] or for which there is "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available."[11] By design, attaching materiality to a disclosure requirement prevents both under- and over-disclosure.

Each reporting company tailors its principles-based materiality disclosures in length, content and detail to its specific circumstances, while line-item requirements ask registrants to report a defined set of information without regard to its relevance to any particular company. Adopting a materiality standard allows each registrant to apply its own judgment to determine what is important to disclose based on management's intimate knowledge of the registrant's specific facts and circumstances – a bespoke disclosure. Generic rules-based standards apply the same disclosure thresholds and requirements (or, at best, provide a handful of discrete threshold levels) to mining companies as they do to retailers, software developers, airlines and manufacturers. While some of these line-item disclosures may be important to a particular

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[6] See SEC, Release Nos. 3310064, 34-77599, "Concept Release on Business and Financial Disclosure Required by Regulation S-K," at 34-35 (Apr. 15, 2016) [hereinafter SEC Concept Release].
[7] SEC Concept Release, *supra* note 6, at 34-36.
[8] SEC, "Interpretation: Commission Guidance Regarding Management's Discussion and Analysis of Financial Condition and Results of Operations" (Dec. 29, 2003).
[9] "The Importance of Independence," Speech of Chair Mary Jo White at the 14th Annual A.A. Sommer, Jr. Lecture on Corporate, Securities and Financial Law (Oct. 3, 2013), http://www.sec.gov/News/Speech/Detail/Speech/1370539864016#.VEasLvnF98E.
[10] Basic v. Levinson, 485 U.S. 224, 231 (1988) (quoting *TSC Industries*, 426 U.S. at 449).
[11] *Id.* at 231–232 (quoting *TSC Industries*, 426 U.S. at 449).

industry or company, they may also be of limited significance to others. Rigid quantitative thresholds may exclude key information from some companies, while imposing substantial compliance expense on others, to produce content with little value.

A significant benefit of applying a materiality standard to disclosure is that, by definition, it should capture emerging issues that are important to a company as they arise without additional regulatory action by the Commission. Likewise, without the necessity of a sunset provision or repeal, disclosure regarding once-important issues naturally drops off as the issues become immaterial to a particular registrant. For example, in the late 1990s many companies faced risks and challenges related to the adoption of the Euro currency and concerns over data integrity and retention due to the Y2K bug. The SEC was able to address both issues through guidance that instructed companies to disclose information on these issues to the extent it was material.[12] Companies disclosed information related to Y2K and the Euro conversion up until the issues were resolved, but were able to omit the information in subsequent years without SEC action. To the contrary, a line-item disclosure remains indefinitely, unless the Commission takes specific action to modify or remove the requirement (which rarely happens). A pitfall to prescriptive disclosure is that it requires the Commission to navigate its complex and time-consuming rulemaking process. Once in place, prescriptive items accumulate in periodic reports, unless the Commission takes affirmative action to "undo" the requirement, resulting in lengthier disclosure that may not assist a reasonable investor in making an informed decision.

Principles-based disclosures deploy the focus and filter of materiality to deliver informative and lean disclosures to investors. In response to questions 7 and 8 in the Concept Release,[13] we encourage the Commission to emphasize a principles-based approach to disclosure, limiting prescriptive disclosure requirements to remove distracting and immaterial information from periodic reports.

Materiality Is Determined by the Needs of Reasonable Investors, Not the Desires of Special Interest Groups

A long-standing tenet of our securities laws has been to target disclosure to items relevant to the decision-making of a reasonable investor. The Commission's rules have been an attractive target for special interest advocates for decades because the rules influence the behavior of the

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[12] SEC, Staff Legal Bulletin No. 6, Publication of Divisions of Corporation Finance, Market Regulation and Investment Management (July 22, 1998) ("An issuer should disclose the impact of the euro conversion if that impact is expected to be material to the issuer's business or financial condition."); SEC, Statement of the Commission Regarding Disclosure of Year 2000 Issues, Release No. 34-40277 (Aug. 4, 1998) ("[W]e believe a company must provide year 2000 disclosure if: (1) Its assessment of its Year 2000 issues is not complete, or (2) management determines that the consequences of its Year 2000 issues would have a material effect on the company's business, results of operations, or financial condition, without taking into account the company's efforts to avoid those consequences.").
[13] SEC Concept Release, *supra* note 6, at 44.

nation's businesses.[14] The Commission has, in our judgment, historically resisted disclosure requirements that are relevant only to a small subset of investors, recognizing that it would be impossible, and in any case undesirable, to require disclosures sufficient to satisfy discrete interests of every investor group.[15] We urge the Commission to continue this measured approach as it considers a number of specialized disclosure additions submitted for public comment in the Concept Release.

Over the years, Congress – often at the urging of special interest groups – has occasionally leveraged federal securities laws to bring public attention to societal concerns, mandating disclosure of information regardless of its materiality or relevance to company performance. A recent example of this tendency is the conflict minerals disclosure mandated by the *Dodd-Frank Wall Street Reform and Consumer Protection Act* (the "Dodd-Frank Act"), which aimed to stop the financing of violent conflict in Africa by requiring companies to disclose their use of minerals from the Democratic Republic of the Congo.[16] Such disclosures are designed to promote laudable societal goals but are largely unrelated to the investing and proxy voting decisions of the investing public. The use of securities disclosures for non-investment goals obscures material information in periodic reports and often delivers only speculative improvements on the societal issue. Indeed, the conflict minerals disclosure intended to aid the Democratic Republic of the Congo ultimately produced an "embargo-in-fact" of the country, choking funds from warlord-owned and legitimate businesses alike.[17] Other regulatory mechanisms are better suited to achieve such goals – mechanisms that do not create barriers to access to capital.

A number of potential disclosure additions discussed in the Concept Release are relevant only to a fraction of investors' decisions or aimed at non-investment societal issues. We urge the Commission to focus on disclosures relevant to reasonable investors broadly and not to adopt such disclosure obligations that would require registrants to track and disclose information that is not material to the company or investor base as a whole.

Sustainability and Public Policy Issues

Concept Release questions 216 through 223 address the addition of mandatory disclosures related to sustainability and public policy issues.[18] Such disclosures may be of interest to some investors, but would not be material to reasonable investors as a group. The societal problems such disclosures would intend to address are likely to be more effectively addressed by other means that require more than reporting and that apply to a broader population than public

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[14] For example, the SEC fielded requests for disclosure requirements related to over 100 societal issues that it evaluated in the 1970s. See generally SEC, Securities Act Release No. 5627 (Oct. 14, 1975).
[15] *Id.* at 7, 18.
[16] *The Dodd-Frank Wall Street Reform and Consumer Protection Act*, Section 1502(a), Pub. L. No. 111-203, 124 Stat. 1376 (2010).
[17] See Letter to President Barack Obama and SEC Chair Mary Schapiro from representatives of the people of South Kivu Province in the DRC (July 5, 2011).
[18] SEC Concept Release, *supra* note 6, at 213-15.

companies. Moreover, companies whose investors are interested in such disclosures can and do make voluntary disclosures outside of periodic reports and, to the extent such disclosure is material to the individual registrant, would be addressed through application of a principles-based materiality standard.

Risk Factors

In response to Concept Release questions 147 and 152, we do not support the suggestion that the rules should require registrants to order their risk factors by perceived significance or highlight significant risk factors in some way. This approach is likely to give rise to litigation given the inherent subjectivity involved in an analysis of importance.

Share Repurchases Issues

Concept Release questions 199 through 204 ask whether disclosures related to share repurchases by registrants should include additional detail and discussion.[19] Existing share repurchase disclosure requirements overlap with U.S. GAAP reporting requirements and offer limited additional value to investors. Furthermore, the lack of a de minimus or materiality threshold on share repurchase reporting requirements can force inclusion of immaterial information in periodic reports. We suggest that no additional detail be required, that only material repurchases require disclosure and that the Commission evaluate the overlap of Item 703's requirements with U.S. GAAP to determine whether any elements of Item 703 could be eliminated.

Subsidiaries Disclosure

Item 601(b)(21) requires disclosure of organizational information of a registrant's significant subsidiaries. Questions 257 through 260 of the Concept Release question whether all subsidiaries, not just significant subsidiaries, should be included in disclosures and whether additional subsidiary-specific information should be provided.[20] Such granular disclosures would add potentially voluminous immaterial information to disclosures and would add complexity and expense to disclosures that are not relevant to most reasonable investors. We strongly encourage the Commission to maintain disclosure requirements only for subsidiaries properly characterized as significant subsidiaries.

Frequency of Reporting

We do not believe the Commission should change the current disclosure regime with respect to the frequency of reporting, as suggested by questions 278 through 285 of the Concept Release. We urge the Commission not to impose more frequent reporting requirements on issuers because the cost of more frequent reporting would be unduly burdensome and there is no

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[19] *Id.* at 193-94.
[20] SEC Concept Release, *supra* note 6, at 254-55.

evidence to suggest that there is a corresponding benefit for investors. We do not believe that investors would benefit from more frequent interim reports given that issuers are presently required to make public disclosure upon the occurrence of certain material events on a more frequent basis. The existing quarterly disclosure regime already places a greater burden on American companies in comparison to some other industrialized nations that require only semi-annual financial reports, such as the United Kingdom. The Commission should evaluate the optimal frequency of reporting in a global context to ensure that American companies are able to compete on a level playing field.

Conclusion

The ultimate point of disclosure is to arm investors with the necessary information to make investing and proxy voting decisions.[21] Mandatory disclosures designed to achieve other goals are inappropriate. The burden of reassessing line-item disclosure on a regular basis to avoid stale or immaterial information is one the Commission – and registrants – should not bear. Refocusing disclosure on material investment information will reduce cost to registrants and the investing public while improving the usefulness and clarity of disclosure.

Thank you for considering our comments and recommendations. We would be happy to discuss our concerns or any other matters that you believe would be helpful. Please contact Maria Ghazal, General Counsel of Business Roundtable, at [redacted] or [redacted].

Sincerely,

John Hayes
Chairman, President and Chief Executive Officer
Ball Corporation
Chair, Corporate Governance Committee
Business Roundtable

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[21] See, e.g., SEC Chair Mary Jo White, National Association of Corporate Directors – Leadership Conference 2013 (Oct. 15, 2013), available at http://www.sec.gov/News/Speech/Detail/Speech/1370539878806#.VJCJIZh0yHs.