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Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Business and Financial Disclosure Required by Regulation S-K (File No. S7-06-16)

Dear Mr. Fields:

CFA Institute[1] appreciates the opportunity to comment on the Securities and Exchange Commission's ("SEC" or "Commission") Concept Release (the "Release") soliciting comments on the business and financial disclosure required by Regulation S-K ("Reg S-K" or the "Regulation"). CFA Institute represents the views of those investment professionals who are its members before standard setters, regulatory authorities, and legislative bodies worldwide about issues affecting the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues affecting the efficiency, integrity and accountability of global financial markets.

Executive Summary

In general, we agree that Reg. S-K is in need of an update that can improve the types of disclosures currently mandated. At the same time, our comments relate more to improvements to current disclosure requirements than to elimination of existing disclosures, as most provide information needed to make informed investment decisions.

We support a hybrid of rules and principles to enhance the quality of mandated disclosures. Data disclosures should tie directly to and reconcile with financial statements, while management should have some leeway in describing how data disclosures reflect registrants' strategic direction and the tactics employed to achieve those goals.

Finally, we believe that technology must play an integral role in any discussion about disclosure reform. Technology should play a role beginning with the capture of data at the beginning of the financial reporting process through to the end of the delivery of financial reports at the end of that process to ensure greater structuring of data and more timeliness of the data.

Discussion

We agree that Regulation S-K could benefit from improved disclosure updates and applaud the SEC for undertaking this review to improve disclosure effectiveness for both issuers and

[1] CFA Institute is a global, not-for-profit professional association of more than 137,000 investment analysts, advisers, portfolio managers, and other investment professionals in 157 countries, of more than 131,400 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 147 member societies in 73 countries and territories.

investors. CFA Institute has provided input to the SEC with regard to the disclosures within Reg. S-X on a number of occasions over the past decade or more. Most recently, we responded to the Commission early in its consideration of its Disclosure Effectiveness Initiative that principally focused on financial and other disclosures required by Reg. S-K, as well as Regulation S-X.[2] In that letter, we urged a number of updates in light of changes in the markets and technology since Reg. S-K was put in place. We also sought to clarify that while certain provisions were in need of updating, investors have not indicated to us[3] that they are overwhelmed by the volume and complexity of existing disclosure. Thus, we encourage consideration of refined and, in some cases additional, disclosure as part of the effort to increase disclosure effectiveness.

We reject an approach biased toward eliminating disclosure as the information disclosures is in nearly all cases of use to investors in their decision-making processes. We reiterate our belief that technology must play an integral role in the discussion of disclosure reform, and support the application of technology to better present financial information to investors in a more efficient and connected fashion, as well as coordinated disclosure requirements with both the Financial Accounting Standards Board and the International Accounting Standards Board.

In the sections below, we respond to the Commission's questions either in bulk or individually.

III. Disclosure Framework

B. Nature of Disclosures Requirements.

What Investors Want from Disclosures. In summary, investors want disclosures that help them understand how changes in the business and competitive environment, the economy, management, and business drivers will affect company performance and financial condition.

In particular, registrants should provide disclosures on the different types of resources that help them generate revenues, cash and profit. Among these resources are the following:

- human resources
- investments in proprietary products
- investments in technological assets
- investments in intellectual property
- investments in trademarks and other intangible assets
- investments in marketing
- distribution networks
- customer lists[4]
- physical assets
- corporate strategies and processes
- financial assets
- financial risks and liabilities
- operating risks and liabilities
- economic and political risks

[2] See November 12, 2014 letter to Keith Higgins, Director of SEC's Division of Corporate Finance from Sandra J. Peters, CPA, CFA and James C. Allen, CFA (the "Nov. 2014 Letter"). https://www.cfainstitute.org/Comment%20Letters/20141112.pdf.

[3] See CFA report *Financial Reporting Disclosures: Investor Perspectives on Transparency, Trust and Volume* (2013); see also condensed version of this report at http://www.cfainstitute.org/ethics/Documents/investor-perspectives-on-disclosures.pdf

[4] The Sports Authority recently sold its customer list to help raise cash for the company's bankrupt corpus.

Even within these broad categories, companies must provide more in-depth info for investors to have a necessary understanding of a registrant's cash-generating (or cash-using) capabilities. With regard to human resources, for example, investors need information about the mix of employees a registrant needs and employs to develop its products and services – engineers, designers, technology experts, manufacturing, assembly, marketing, finance, administrative, etc. – rather than a total number of employees. The benefit to investors from this type of information is that they can determine whether a company's current employees matches the mix of employees that is optimal, and the location of staffing to operate profitably into the future. For example, information about how many aerospace engineers employed by an aircraft manufacturer versus the number of administrative staff would indicate how well the company is situated to develop new and competitive products and services for the future.

Likewise, a list of patents without relevant expiration dates, could lead to false sense of security for some investors, or a valuation discount for others. Providing the greater context to such matters is necessary to enable investors to comprehend and calculate the remaining value of such intangible, intellectual assets.

The list above is a list of common business drivers, but individual firms may have others, or unique combinations of drivers for their businesses. It is therefore futile and limiting for the Commission to try to provide a list of these factors. Rather than a prescriptive list of possible business drivers that companies should describe, a principle-based approach, in this case, calling for descriptions of the material business drivers for each registrant would provide a more useful approach. We discuss the relative needs for principles-based and prescriptive disclosures in the next section.

Qs 1-5: Sun-Setting of Statutory Mandates

As noted below in our discussion about the audience for Reg S-K disclosures, we believe the Commission should create disclosures with equity investors in mind, as they are owners of whatever residual value of a company remains after an issuer's debts are paid and assets liquidated. They, more than anyone, need information to help them determine whether investing financial assets for their clients, or for their own benefit, is warranted. Unlike short-term creditors whose debts are paid within a few months, or even long-term debt investors, whose securities mature 15 years or even 30 years after issuance, equity investors' interests in a company will last as long as the company is in business. By making disclosures attendant to these types of investors, the Commission will satisfy the information needs of all stakeholders.

Because of the perpetual nature of shareowners' and equity investors' interests, and because disclosures should be created with equity investors and shareowners in mind, we do not believe that most disclosures should be sun-set. The risks of an issuer will likely evolve over time, for example, causing disclosures about some to disappear and others to appear. To sunset risk disclosures, however, because some have abated would ignore the emerging risks a company faces as its business environment changes. Therefore, sun-setting would not serve investors' interests.

We recognize that the Commission could, from time to time, mandate disclosures on matters that are fleeting in nature. These could benefit from sun-setting. Examples might be the risks associated with implementation of new mileage regulations for automakers over the next 10

years. Such disclosures should be recognized as temporary at the time of mandate, and a specific sunset date should be incorporated. Most disclosures under consideration within this Release, however, would not and should not fall into the category of disclosures needing to sunset.

Qs 6-13: Principles-Based and Prescriptive Disclosure Requirements.

CFA Institute has been a strong proponent of prescriptive standards with regard to financial reporting because registrants have shown a tendency to interpret principles in a manner that is most beneficial to them rather than most beneficial to investors. In general, principles-based requirements will have one, some, or all of three primary outcomes. First, issuers will withhold disclosure based on an internal determination that the information is immaterial. Second, issuers will group information in a manner that obfuscates negative performance or conditions. And third, different issuers will apply the "principles" differently, thus making the information incomparable across different issuers.

For data-driven disclosures, therefore, we believe the Commission needs to provide prescriptive rules as to what must be reported, the manner in which it is reported, and the assumptions behind the reporting. As noted above, without such prescription, investors may not receive materially important information, may not be aware of material information, and/or they would not be able to compare disclosures across companies or across industries.

With regards to regulatory disclosures that supplement the financial reporting of an issuer, on the other hand, we believe a hybrid approach is needed to satisfy the disclosure needs of investors. As noted in our Nov. 2014 Letter, a principles-based approach to capital and liquidity disclosures in banks' MD&As prior to the 2008 financial crisis did little to provide investors with the data needed to analyze such firms. Also as noted in the Nov. 2014 Letter, a principles-based approach doesn't bode well with the development of technology and the structuring of consistent data within and between companies. And finally, there is nothing preventing companies from providing additional principles-based disclosures to supplement prescriptive disclosures. Many companies do this by reporting adjusted earnings per share, though such information highlights the need for standards as the information is not comparable across companies or even across industries.

On the other hand, for many qualitative disclosures, including many discussions within the Management Discussion & Analysis ("MD&A") and the Compensation Discussion & Analysis ("CD&A") that supplement data disclosures, a principles-based approach may be applicable. The reason is that each registrant will have a different strategy, and different internal tactics to execute its strategy. Issuers should have an opportunity to describe those elements of their businesses in the manner in which they believe best conveys the essence of their efforts.

A good example of this approach is presented in the Compensation Discussion and Analysis Template[5] (the "CD&A Template") that CFA Institute put together with the assistance of a group of issuers, investors, corporate secretaries and corporate governance experts. In the CD&A Template, companies are encouraged to provide context around and about the required tabular disclosures mandated in the CD&A by the SEC. In these cases, companies have the freedom to tell their stories in the contextual parts of the CD&A, whereas a rules-based approach has led to a box-ticking approach with boilerplate disclosure. A rules-based approach with regard to

[5] See http://www.cfapubs.org/toc/ccb/2015/2015/4. Updated and released in April 2015.

disclosures similar to those of the CD&A and MD&A, can lead to issuers only meeting the minimum standard with boilerplate disclosures.

Even within this principles-based structure for qualitative discussions and analyses, however, we believe it is imperative that any financial information should be tied back to and reconciled with the financial statements provided in accordance with appropriate financial reporting standards. If registrants seek to create their own metrics for operating earnings, for example, they should have to provide operating earnings as presented in the financial statements first before the proprietary metric, and follow that with a reconciliation back to the financial statement number. Without this requirement, companies could resume the practice begun in the heyday of the tech / telecom / internet boom of the late 1990s, when companies engaged in diversionary metrics that had no relevance either to the financial statements or their competitors.

A principles-based approach, then, where appropriate, will allow issuers to tell their unique stories and address the issues and factors unique to their industries/sectors. This allows both investors and issuers to focus on the business drivers, risks and opportunities unique to their situations without getting bogged down in boilerplate that complies with hard-and-fast rules. Finally, we repeat our Nov. 2014 Letter suggestion that the SEC examine the degree to which financial information is sourced directly from SEC filings or from data providers, as well as user preferences about the construction and delivery of the financial information.

Materiality. With regard to the question of materiality, we begin with the perspective that any definition should have investors' views as its central concern. We also agree that materiality determinations cannot be reduced to numerical formulas.

Ultimately, we do not see any reason for the Commission to change its definition of "material," as described in the 1982 revision of Rule 12b-2 pursuant to the Supreme Court's determination:

> "*Rule 12b-2 of the Exchange Act provides that the term 'material,' when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters to which there is a substantial likelihood that a reasonable investor would attach importance in determining whether to buy or sell the securities registered*."

2. Audience for Disclosures: Qs 14-20

The Commission enquires about who it and issuers should assume are the consumers of the information provided in their Reg. S-K disclosures. We reiterate the position proffered in the Nov. 2014 Letter. In particular, we stated "that sophisticated investors are likely the most appropriate audience for SEC filings as they are generally those investors doing the detailed analysis and acting as price-makers."

A 2013 survey from the Pew Charitable Trusts[6] supports this view. That survey found that just 45% of people nationwide had money invested in the equity markets, with 77% of college grads saying they invested in the equity markets. By comparison, 45% of those with some college, and just 25% without any college education said they invested in the equity markets. On the basis of

[6] http://www.pewresearch.org/fact-tank/2013/05/31/stocks-and-the-recovery-majority-of-americans-not-invested-in-the-market/. It is unclear how many of the respondents who said they did not have money in the stock market were benefiting from a pension fund at the time. Nor did the survey indicate whether respondents invested in individual equities or in mutual or exchange-traded funds.

income, the survey says that 80% earning more than $75,000 invest in equities, compared with 55% earning between $30,000 and $75,000, and just 15% earning less than $30,000.

At the same time, the Investment Company Institute reports in it "2016 Investment Company Fact Book" that more than 93 million individuals owned interests in mutual funds, or nearly one in three U.S. residents. This suggests that many of those telling Pew they invested in equities are doing so through mutual and exchange-traded funds and thereby relying upon professional managers to make their investments for some or all of their investment portfolios.

Based on this information, we believe that the most regular audience for both the financial statements and supplementary disclosures mandated by the Commission are the following:

- Equity securities analysts
- Fixed-income securities analysts
- Credit ratings analysts
- Institutional investors
- Competitors
- Academics
- Economic policy-makers
- Regulators
- Suppliers
- Customers
- Retail "DIY" investors

Ultimately, we reiterate our long-standing perspective that disclosures considered throughout this Release should be geared toward the information needs of equity investors. These are the people who hold the residual interests of any company and, therefore, have greater information needs that any other constituency. If their information needs are satisfied, the needs of all other stakeholders will have their informational needs met, as well.

IV. Information for Investment and Voting Decisions

A. Core Company Business Information

1. General Development of Business (Item 101(a)(1)): Qs 24-30

Q 27. We would support inclusion of a registrant's business strategy, but we do not support another SEC mandate to achieve this goal. This is a disclosure that companies should want to provide. They should want investors to know and understand their strategies and how the financial statements, investments and even compensation strategies all reflect those corporate strategies.

2. Narrative Description of Business (Item 101(c)): Qs 31-41

Q 31. We believe that Item 101(a)(1) is particularly important for investors in emerging growth companies ("EGCs") and small reporting companies ("SRCs"). How long a company has been in existence is relevant to investors' considerations as to the experience of management, insider ownership, customer and supplier diversification, and cash flow considerations, among others.

Disclosures related to how an organization was structured 150 years ago, on the other hand, will have little relevance to current investors, and therefore are not necessary beyond the state of incorporation. Nevertheless, changes in corporate structure, the nature of a firm's or its primary subsidiaries' businesses, and any mergers, acquisitions or divestitures are very important to investors.

Q 34. Disclosures about an issuer's industry are not as important as descriptions of the competitive environment within which that issuer operates. These days, companies must compete not just with companies operating within their industries but also with entities external to the presumed industry segment. Technological advances, for example, have changed competitive landscapes for companies in a variety of industries, and therefore may pose bigger threats to registrants than those within its "official" industry classification.

Therefore, we strongly support a broader disclosure that covers the competitive landscape rather than just an issuer's industry.

Qs 36/39. The list of 13 disclosure items provided in Item 101(c) are consistent with the list of business drivers noted in our response to "What Investors Want" beginning on page 2 above. While not a complete list of potential drivers, the list in the Release covers such a number of relevant factors, together with requiring discussions about competitive, environmental and customer risks. In this case, the description of qualitative factors of this sort would benefit from a principles-based approach that broadens the discussion to cover all relevant business drivers and risks.

Q 37. We would accept a rule that required Item 101(c) disclosure in an issuer's initial filing, while limiting follow-up disclosure in periodic reports to material changes under two primary conditions. First, the Commission should enforce a narrow definition of the term "material" to ensure that important changes are reported in a timely and substantive manner. This should include guidance to issuers and the preparer community regarding this definition to ensure greater compliance and more substantive and timely disclosures. Second, disclosure of 101(c) information should be included in all new offering documents — such as post-IPO debt and equity offerings — to ensure new investors in an issuer's securities are aware of these basic corporate facts.

3. Technology and Intellectual Property Rights (Item 101(c)(1)(iv)): Qs 42-46

Qs 42-44. We absolutely believe the Commission should retain Item 101(c)(1)(iv)'s disclosure of registrants' patents, trademarks, licenses, franchises and concessions, as these often are important drivers for registrants' businesses. We also support including copyrights under this disclosure requirement, as creation and ownership of content is an increasingly important means of attracting advertising revenue, subscriptions, advertising, and other sources of income for companies. We support the idea of a tabular disclosure that separates intellectual assets by asset type (patent, trademark, copyright, license, etc.) and disclosure for individual assets that are material to the issuer's business plan. The tables should describe the asset, its purpose, and expiration date of each.

Q 45. We do not support limiting these disclosure requirements to registrants in particular industries, largely because it is nearly impossible for the Commission to determine which will or will not develop intellectual property that alters an industry's structure. As for where these disclosures should occur, we believe that, in general, the discussion relating to these assets should be part of the business description section. At the same time, changes in the composition of an issuer's portfolio of intellectual assets, and threats to the value of such assets would, we believe, warrant reference (to the discussion in the business description section) in sections relating to trends and developments and risks.

4. Government Contracts and Regulation, including Environmental Laws (Items 101(c)(1)(ix) and (c)(1)(xii); Qs 47-48

b. Government Contracts (Item 101(c)(1)(ix): Qs: 47-48

Q 47. Disclosures relating to government contracts would be important for investors if such contracts constitute a material part of a registrant's business. These should be disclosed as part of a table listing all material contracts, but described separately given the potentially unique features of such contracts.

c. Compliance with Environmental Laws (Item 101(c)(1)(xii): Qs: 49-53

Q 49. There is increasing focus on how different environmental, social and governance (ESG) factors can influence the long-term viability of a registrant. Many of the factors that investors consider and companies measure are not covered in any current law. Moreover, the relevant issues will vary on an industry-by-industry, and in some cases on a company-by-company, basis.

We therefore encourage the Commission to work with investors and issuers to focus on those ESG issues that are material to specific industries and include that information in the industry guides discussed in section IV.E. of this Release. The goal should be to ensure that adequate measurement, authentication and disclosure of these factors are undertaken by issuers so that investors can have a full understanding of the long-term potential for the companies in which they invest.

Q 50. We believe that information relating to the material effects of compliance with regulations controlling the discharge of materials into the environment or otherwise protecting the environment is important to questions of sustainability, risk and long-term profitability. Therefore, they should be disclosed.

Q 51. To the extent that the effects that other regulations may have on a registrant's capital expenditures, earnings and competitive position are material and are measureable and knowable, they should be disclosed.

5. Number of Employees (Item 101(c)(1)(xiii)): Qs 54-59

Q 54. The number of full-time equivalent employees and part-time employees are important data points, but must be put in the context of registrants' business plans and business drivers, as noted on page 2 in our discussion, "What Investors Want from Disclosures." For example, investors would benefit from knowing whether a registrant whose business plan relies on the development of new technologies has the number of engineers, and the

right kind of engineers it needs. Likewise, investors would benefit from knowing the relative number of line personnel engaged in production versus the relative numbers engaged in unproductive activities. Once again, investors are interested in understanding the business drivers for a registrant and how consistent these are with its business plan.

Q 57. While we believe a range of staff is fine — the number of employees leaving and arriving makes a finite number nearly irrelevant — the Commission should use a narrow range to avoid ranges greater than plus or minus 3%. Further, we believe any discussion, whether relating to ranges of employees or actual numbers, should still discuss whether these numbers are consistent with registrants' business plan needs for specific types of employees.

6. <u>Description of Property (Item 102): Qs 60-66</u>

Qs 60-61. Item 102 relates to disclosures about the location and general character of principal plants, mines, physical properties, etc. Whereas the nature of business has changed over the years, from one where physical assets represented many registrants' principal business drivers to one where intellectual assets are often more valuable than the buildings where those assets are developed, we believe disclosures relative to such physical assets remains relevant. For one thing, even for technology firms, these remain material assets that may be sold in bankruptcy. For more traditional industrial firms, such properties remain important drivers of their business models and therefore warrant disclosure, as well.

We believe these assets should be cross-referenced against relevant financial capital reported in the financial statements, including debt, capital leases and intangible assets, together with acquisition costs, amortization, depreciation and on-going annual maintenance costs.

B. Company Performance, Financial Information and Future Prospects

1. <u>Selected Financial Data (Item 301)</u>

b. <u>Five-Year Trend Data (Instruction 1): Qs: 67-75</u>

Qs 67-70. We believe that investors absolutely benefit from five years of selected financial data. Five years is more likely to capture the effects that business cycles may have on a registrant's business model than a shorter period would. Without this disclosure, moreover, investors would have to refer to prior-period reports, which may not be comparable to the reporting standards used in more recent reports. Consequently, investors would have a difficult time comparing and contrasting current period reporting with how a registrant has evolved — positively or negatively — over the intervening period.

Q 71. Whether all registrants should benefit from an exemption from presenting selected financial data prior to the earliest audited period with regard to its first effective registration statement seems unreasonable. Such an exemption currently applies to emerging growth companies ("EGCs") largely because they are typically start-up companies that only began having audits of its financial statements prepared prior to registration for a public offering of its securities.

Besides EGCs, entities most likely to benefit from such an exemption would be privately owned firms preparing to reenter the public markets through an initial public offering. Other possible entities would be those reentering public markets after a bankruptcy reorganization of their debts. In either case, such firms will have had operations that extend well beyond the most recent period receiving an audit that would give investors a better indication of how a registrant will perform over a longer period of time.

To reiterate, investors would benefit from knowing how such registrants' operations have evolved and changed over time. We therefore, do not support revising trend data rules for operating registrants to the lower EGCs' standard.

Q 74. The audience for this type of trend information is no different from the audiences noted above in response to Qs 14-20.

c. Items Included in Selected Financial Data (Instruction 2): Qs 76-78

Q 76. The financial information provided in the selected data tables must be accounted for in a standard manner to enable comparability. While non-GAAP disclosures may be useful to investors, without relevance to GAAP these data could be misleading. Consequently, we believe disclosures required under this instruction should include presentation of GAAP-based data, and an explanation of how the non-GAAP data relates to the GAAP data.

2. Supplementary Financial Information (Item 302): Qs 79-87

Q 79. The only change we would suggest for Item 302(a) relating to selected quarterly financial data about operations would be to ensure that the information is presented in a consistent manner.

Q 81. Cycles are shorter than when Item 302(a) was introduced as the pace of change in and competitive nature of some sectors of the economy has increased. That doesn't mean, however, that this information isn't relevant anymore. On the contrary, if anything it is more relevant than ever. Quarterly reporting on such matters is sufficient to meet investors' need for periodic updates on performance and financial condition.

Q 82. While the use of non-GAAP financial measures to describe performance can be useful to investors, it can also mislead investors regarding a company's financial condition, liquidity and performance. For example the *Wall Street Journal* reported that 40 companies with initial public offerings (IPOs) in 2014 showed losses under standard accounting rules (i.e., GAAP), but they reported profits using adjusted and/or customized performance measures or non-GAAP measures. This could potentially mislead investors. In light of the proliferation in the use of non-GAAP measures and growing investor concerns, CFA Institute commends the SEC for issuing its guidance regarding the use of non-GAAP measures, including specific examples of inappropriate adjustments to GAAP measures and illustrations of presentations giving greater prominence to non-GAAP measures.

The Concept Release asks whether external auditor review should be required of the measures used to portray financial performance. We favor requiring such external auditor

review, given the potential for non-GAAP measures to mislead investors by distorting the portrayal of financial results and financial condition of a registrant.

3. Content and Focus of MD&A (Item 303): Qs 88-98

The MD&A has three primary objectives for investors, namely to:

i) provide an explanation of the financial results and statements from management's perspectives;

ii) to enhance the disclosure of relevant information and provide additional context to the financial statements; and

iii) iii) to provide context about the quality of earnings and about earnings variability.

As noted above, we believe this information should be provided subject to a rules-based regime when regarding quantitative discussions and presentations of operational results and financial condition, and that these data should be consistent with and tied to the audited financial statements. Issuers should be granted greater leeway in the way in which they provide qualitative context to performance and condition, so long as these discussions aren't misleading or omitting important and material information.

Below are our responses to the issues posed by the Commission with regard to Item 303 generally:

Q 88. What is most important to investors, analysts and other users of financial statements are the factors that drive issuers' businesses. These are described in "What Investors Want from Disclosures" beginning on page 2.

Q 89. Without disclosure about this information, a registrant could create significant off-balance sheet liabilities that have the potential to impair its financial condition without investors knowing of it. In this case, a company could merely state that it has no on- or off-balance sheet debt if that is the case. Consequently, we believe such disclosures are needed.

Q 90. Yes, consolidation of Commission guidance on MD&A would be helpful and could lead to more consistent application of that guidance.

Q 91. We support a layered approach to Item 303 disclosures in so far as issuers are required to include "negative" information in their determination of what is "most important." Specifically, we don't want this approach to lead to a filtering process in which the "most important" information and analysis includes only the most beneficial information and analysis about an issuer, while ignoring negative information. Secondly, it will require additional time and effort from management that could be devoted to better disclosures elsewhere in the MD&A.

Q 95. We wholeheartedly support the tagging of information disclosed within the MD&A.

c. Forward-Looking Information: Qs 99-102.

Q 99. We believe the current two-step test considering the likelihood of a known trend, demand, commitment, event or uncertainty, and the need for management to objectively

evaluate the consequences of the trend, etc. if it cannot make that determination, is preferable to the Supreme Court's "probability/magnitude" test.

d. Key Indicators of Financial Condition and Operating Performance: Qs 103-106.

Q 103. Consistent with the discussion near the beginning of our response regarding "Principles-Based and Prescriptive Disclosure Requirements" beginning on page 3, we support a hybrid approach to Item 303 disclosures relating to performance metrics. In particular, metrics relating to performance and financial condition, including information presented in tabular form, should adhere to established disclosure rules and reconcile with a registrant's financial reports.

The narrative providing context around the data should be principles-based to enable registrants the opportunity to tailor their message to their strategies and their particular situations. It is relevant to investors to see what management says are its key performance metrics, so long as the disclosures are supplemental to more traditional metrics. The discussion above about the CD&A is an example of the blending of principles- and rules-based disclosures.

Q 106. A good way to determine the key metrics for an industry is to see what matrices companies within an industry use in their regulatory and non-regulatory reporting.

4. Results of Operations: Qs 107-112.

The disclosures mandated in Item 303(a)(3) are intended to alert investors to operational changes in four key areas:

- unusual or infrequent events or transactions, or economic changes that materially affected performance of continuing operations
- trends or uncertainties that could materially affect revenues or income from continuing operations
- material changes to revenues, with attribution given to price changes, changes in sales volume, or introduction of new products or services, and
- the effect of inflation on revenues and income over the prior 3 years.

Q 107. This type of information is of vital importance to investors, as it provides an indication of whether a registrant's revenue growth is a function of improved product/service sales, higher prices, or some combination of both.

Q 108. Inclusion of a discussion about changes resulting from competitors emanating from outside a registrant's industry should be provided, but as part of a delineation of competitive threats within the risks section of the MD&A.

Q 109. While most investors are capable of making their own three-year comparisons of revenues and income, what is most useful to Item 303(a)(3) disclosures are the comparisons of continuing operations and the relative effects of inflation versus growth in number of products or services. These would be more difficult to find, organize and consolidate into one table, particularly for retail investors. Consequently, we support retaining this disclosure.

Q 112. Item 303(a)(3) disclosures could provide useful information about entities who have yet to generate revenues. For example, such information could be useful in determining the cash-burn rate for such companies. Additional disclosure about the registrant's operating plans should already be included in Item 101(a), while a discussion of how close a company is to generating revenue and earnings could be part of this Item.

5. Liquidity and Capital Resources (Item 303(a)(1) and (a)(2)): Qs 113-120.

Q 113. Prompting more meaningful disclosures regarding liquidity and capital resources while permitting registrants to analyze these factors in the context of their own businesses will require companies to describe "how" and "why" changes to these factors occurred or didn't occur. It should go beyond a discussion of "what" happened and "how much" something changed.

Q 114. We do not see liquidity and capital resources as synonymous and therefore do not support the combination of the two. Liquidity relates to cash or near-cash assets such as accounts receivable, marketable securities, and other holdings that are short-term in nature. Capital, in this sense, relates to longer-term sources of funds that have been invested in the business. Capital resources that may be in cash or near-cash form typically relate to raised funds waiting to be invested in productive capacity or, in the case of retained earnings, are held for dividend payments or share repurchases. Either way, we believe these items should be disclosed and discussed separately.

Q 118. Sensitivity analyses should be reserved for registrants whose liquidity and capital are significantly affected by short-term changes in asset prices. Banks and other financial companies whose holdings' fair market values vary on the basis of changes in interest rates are prime examples of registrants whose disclosures should include sensitivity analyses.

Q 119. Again, we believe the type of disclosures relating to intra-period liquidity and capital would be beneficial coming from registrants whose assets and liabilities are sensitive to changes in economic factors like interest rates. The purpose of such disclosures, we believe, would be to capture gaming of period-end liquidity or capital metrics in the way that Lehman Bros. manipulated its financials in the year prior to its bankruptcy.

Graphic presentations would be beneficial, where applicable, as supplements to numeric disclosures. And measures such as average daily assets should highlight disparities in period-end and intra-period liquidity and capital.

Short-Term Borrowings: Qs 121-124

Q 121. Instruction 3 to Item 303, like Item 303 itself, relates to trends, events and significant changes to a registrant's liquidity or short-term borrowing capacity. These are relevant and important disclosures, and we support their inclusion in Item 303(a)(1) disclosures. We also prefer the tabular disclosure and narrative discussion of short-term funding sources as originally proposed by the Commission in 2010. This section should cross-reference its disclosures with information on short-term borrowing included in the Notes to the Financial Statements section of the audited annual financial reports, and the unaudited quarterly financial reports.

Q 123. Given the increase in short-term borrowing at non-financial institutions as a consequence of low interest rates, we support application of tabular presentation and narrative discussion of short-term borrowings for such enterprises going forward. Naturally, the factors cited in these disclosures will be different than the disclosures for short-term borrowings applicable to financial institutions. And while we support disaggregation of amounts in the proposed tables for non-financial and financial firms, alike, we believe the proposed threshold of 30% of shareowners' equity may reduce the visibility of important funding mechanisms. Consequently, we suggest a threshold of around 10% of total capital, defined as the sum of long-term and short-term debts, preferred shareowners' equity and common shareholders' equity. No chart is needed.

6. Off-Balance Sheet Arrangements: Qs 125-130

Q 125/128. The disclosures in Item 303(a)(4) are of critical importance to shareowners and absolutely should be retained. If anything, these disclosures should be expanded in line with the suggested disclosures included in our letter to the Commission dated 28 April 2014, which itself was a reiteration of suggested disclosures included in several letters to the Commission dating back to 2004[7] (the "ABS Disclosures Letters"). These disclosures should go beyond what is required for disclosure in the Notes to the Financial Statements and should include the following ongoing disclosures:

- Static pool disclosures, including narratives describing the methodology used to determine the characteristics of static pool information, and how assets in pools differ from each other
- Issuers should provide graphic representation of static pool data for delinquencies, losses, and prepayments for amortizing trusts
- Revolving master trusts should disclose delinquencies, monthly payment rates, prepayments and losses by vintage year and credit score
- Static pool disclosures should be provided in formats such as XBRL, but not in .pdf files, to enable investors to quickly access and apply analytical tools
- distribution of assets by geographic location
- distribution of assets by credit score of the borrower
- distribution by type of asset (car, truck, make, model; or home equity vs. first mortgage);
- distribution by loan-to-value ratios
- percentage of loans originated in-house versus those originated by third parties
- list of largest originators by dollar volume originated if more than 10 percent originated by third parties; and
- to-date delinquency and default information about loans in the pool, among other things.

[7] Response to, "Re-proposal of Shelf Eligibility Conditions for Asset-Backed Securities and Other Additional Requests for Comment http://www.sec.gov/comments/s7-08-10/s70810-235.pdf submitted on 9 November 2011; Response to, "Asset-Backed Securities," http://www.sec.gov/comments/s7-08-10/s70810-151.pdf, delivered 20 August 2010; and Response to: "Asset-Backed Securities, http://www.sec.gov/rules/proposed/s72104/cfai071504.pdf, delivered 15 July 2004.

7. Contractual Obligations: Qs 131-136

Q 133. Contractual obligations will differ on a case-by-case and company-by-company basis. We therefore recommend requiring a narrative to compare these obligations beyond the top-line disclosures provided in the financial statements and in the Item 303(a)(5) tables.

C. Risk Factors: Qs 145-156

We believe issuers must provide an understanding of the linkage of each risk the registrant delineates against the relevant business drivers described in Item 101 that are affected. Likewise, registrants should describe the risks in an entity-specific manner by categorizing them in terms of their nature, assessing them for significance and connecting them to financial results such that they can be priced.

Q 145. We support the suggestion in the Release of calling for a discussion to accompany each risk disclosed by a registrant. Such narrative should include a discussion of how the registrant is addressing each risk.

Q 146. In general, if a known trend, demand, commitment, event or other possible event is unlikely to occur, then no disclosure is needed. Moreover, any discussion of probability is likely beyond the control of management to predict. For example, automakers faced significant sales declines and eroding financial conditions as a consequence of the global financial crisis of 2008/2009. While each may have warned of a downturn prior to that time, their knowledge of when the downturn would begin, its severity or would have been guesswork. Consequently, we don’t believe such information will be useful to investors.

On the other hand, investors would benefit more from understanding the potential severity that the occurrence of a specific risk might have on the performance and financial condition of a registrant. If the potential severity is material, it should be disclosed.

Q 147. We believe that calling for a narrative about each risk (Q145), and a discussion of the potential severity of each (Q146) should yield information that investors will find useful.

Consolidated Risk-Related Disclosure: Qs 180-182

Q 181. A consolidated discussion of risk factors would enable investors to see in one place, not only the material competitive, financial, economic, operational and legal risks a registrant faces, but also would provide the means by which the registrant is working to manage those risks. A discussion of the greatest risks facing individual registrants could be incorporated here by ranking the risks in order of greatest to least important.

D. Securities of the Registrant

Related Stockholder Matters – Number of Equity Holders (Item 201(b)): Qs 183-185

Q 184. Disclosures about the number of shareowners has continuing benefit to investors in that it shows how widely an issuer’s shares are owned. Nevertheless, the prominence of share-ownership by virtue of ownership in shares of mutual, exchange-traded and hedge funds, together with securities held in “Street” name does lead to an understatement of the breadth of investor interest, if not ownership rates. Therefore, it would be useful for

investors to know the percentages held by marketable investment funds, by individuals, by insiders and in "Street" name. Such information can give investors a sense for how mass redemptions and other events at select investment funds that are beyond the performance of a registrant could affect share prices.

Purchases of Equity Securities by Issuer and Affiliated Purchasers (Item 703): Qs 199-204

Q 199. Information regarding the number of shares a registrant or affiliated entity has repurchased, the average price per share paid, and the maximum number of shares a registrant may repurchase pursuant to an active repurchase program is of significant importance to investors. Such disclosures should be accompanied by a narrative discussion about the source of the funds used to make the repurchases and how this will affect registrants' indebtedness, if at all.

Shareowners and investors also would benefit from understanding the relation between the amounts spent on buybacks and the decision-making and governance processes that guide capital expenditures. Repurchases reflect management's investment priorities, or lack of alternative investment opportunities in research and development, marketing, dividends, property and equipment, intellectual property or technology, for example.

E. Industry Guides: Qs 205-215

Q 205. In our DEI Letter, we said industry guides remain a relative disclosure tool and provide the opportunity to present a more complete/cohesive picture of a business for a range of industries. At the same time, we said they should be updated to reflect disclosure changes in S-K and contents of underlying financial statements. We also believe there is room for improvement with regard to the nature of the industries covered, the requirements in the guides relative to U.S. GAAP, and the integration of disclosures required by the guides and those related to risks, market risks and MD&A. We believe the Commission should look to standards set by the Suitability Accounting Standards Board and the International Integrated Reporting Council for indications of what types of information is most relevant.

F. Disclosure of Information Relating to Public Policy and Sustainability Matters; Qs 216-223

Q 216. The sustainability issues that are important to informed voting and investment decisions will vary by sector/industry. It is imperative that the SEC develop disclosure requirements that require companies to disclose material sustainability information while allowing issuers the flexibility to disclose that which is germane to their industry/sector without having to worry about required disclosures that do not apply to them.

Q 217. We do not believe that line-item requirements for disclosure of sustainability issues would be beneficial to issuers and investors, as what issues are material will differ by industry/sector.

Q 218. The sustainability reports produced by issuers can be helpful, but what they consider will differ greatly even within the same sector/industry. It is therefore imperative that the

SEC work with issuers and investors to set guidelines on an industry-by-industry and sector-by-sector basis for what information is material and what is not, so that issuers and investors both can save time and resources in producing and reading such disclosures. In particular, the Commission should consider the work done by organizations such as the Sustainability Accounting Standards Board, which has specified voluntary, industry-specific disclosures, or others, such as the International Integrated Reporting Council.

Q 220. While many environmental and social factors will vary by industry, governance factors of interest to investors are generally comparable across firms, with some exceptions for size of firms and industry lifecycle. Any line-item disclosures concerning corporate governance issues of interest to investors that are not currently covered by the current disclosures would fall into this category.

Q 221. As noted above, many issuers already provide lengthy sustainability or ESG reports to their investors, so many issuers will not face a new and burdensome cost by collecting, verifying and disclosing ESG information. However, costs may be saved if instead of producing large sustainability reports that cover a broad range of sustainability information, issuers can instead focus on only collecting, verifying and disclosing information concerning the factors that are material to them and their investors.

Q 222. We believe that all issuers should be held to the same disclosure standards on sustainability and public policy issues.

G. Exhibits

Subsidiaries and Legal Entity Identifiers: Qs 257-260

We believe the SEC should explore the use of Legal Entity Identifiers (LEIs) raised in the Release with the goal of increasing investors' ability to identify and analyze risks of registrants and their subsidiaries. We agree with the Investor Advisory Committee (IAC) that financial firms are not the only registrants using complex structures and that LEIs should not be limited to those firms.

H. Scaled Requirements

Categories of Registrants Eligible for Scaled Disclosure: Qs 264-267

Q 264. We concur that EGCs and SRCs that have failed to file reports with the Commission, regardless of whether they are shell companies or are not guilty of violating anti-fraud sections of federal securities laws, should not benefit from the reduced disclosure and governance requirements available of the scaled disclosure regime. While these sanctions may make it less likely that such registrants can meet the requirements to benefit from scaled disclosure, we believe such sanctions are needed to create an incentive for EGCs and SRCs to meet even these reduced reporting and governance mandates.

Q 265. We believe the scaled reporting structure described in the Release has created a dual-regulatory system that many, if not most, investors are unaware exists or what it covers.

Nor is it easy for investors to determine which registrants are taking advantage of the scaled requirements, and which are not.

To overcome this informational asymmetry, we encourage the Commission to enhance disclosures to enable investors to distinguish between those registrants using the scaled disclosure regime and those that are not. Such registrants should have to disclose this fact among the list of risks the company and its investors face.

We have previously articulated our views regarding differential reporting requirements with respect to private companies stating that investors will factor the differences (i.e. they will price the lack of transparency, clarity and comparability into what may be perceived to be lower-quality requirements) into their price determinations. Our views would be similar for a more scaled disclosure regime.

Frequency of Interim Reporting: Qs 278-285

Q 278. In "Breaking the Short-Term Cycle"[8] (the "Short-Termism Report"), a report published jointly by CFA Institute and the Business Roundtable Institute for Corporate Ethics, it was determined that short-termism in the securities marketplace isn't caused by quarterly reporting. While calling for changes to pay incentives, poor leadership, and communications and transparency, most relevant to the discussion raised here is the issue of earnings guidance. Specifically, the report called for issuers to end the practice of earnings guidance, which has been found to cause companies to forego investments in research and development, in marketing and other value-creating initiatives so that they could meet their earnings targets. The Short-Termism Report suggested that issuers adopt an approach that takes a longer-term perspective to the guidance provided, looking at long-term value creation of current investments.

Unlike guidance on quarterly earnings, *ex post* reports on registrants' operating performance and financial condition are very definitely valuable to investors and must be retained. They are an important means of keeping investors informed about changes in performance and financial condition near to the occurrence of events that may affect long-term value. Decisions about existing and new investments are not made just once or twice per year but on an on-going basis. Without information that is timely, external investors are at an even greater disadvantage to insiders in their ability to respond to relevant information.

V. Presentation and Delivery of Important Information

G. Structured Disclosures: Qs 330 - 340

In our 2013 report, *Financial Reporting Disclosures: Investor Perspectives on Transparency, Trust & Volume,* we noted that today's financial reporting system is based on paper and associates higher word or page counts with increased complexity. We also note that this approach neglects

[8] http://www.cfapubs.org/toc/ccb/2006/2006/1

the ways that data and technology can improve the quality of information and investors' access to it because it presumes that information is consumed by humans, and therefore must be presented in a manner that humans can consume rather than in a machine-readable format.

The report highlights that technology must be an integral element of the discussion on disclosure reform. The excerpt below states that the future will need to consider how technology can be utilized, not only at the end of the financial reporting process but at data capture, to ensure greater structuring and timeliness.

> *Investors believe the conversation about disclosures specifically and financial reporting more broadly needs to consider the vast changes in technology that have occurred in the past 10–20 years. The conversation needs to consider how technology can be effectively leveraged to provide the information investors need for investment decision making in a globally connected, data-driven economy. Investors do not seek a reduction in data or volume of disclosures as they have the ability to utilize technology to evaluate the data. Identifying ways to effectively capture, manage, analyze, present, and deliver financial data is the reform investors see as necessary.* ***How technology can be harnessed to reform the financial reporting process end to end—not simply in the filing of documents with regulators as in the case of EDGAR and XBRL—is where investors believe the dialogue on disclosure reform should be focused.***

SEC Filings

CFA Institute believes that a single XBRL filing should be the mandatory format for reporting. Dual filing in both PDF (portable document format) and structured formats does not fully bring about the efficiencies afforded by XBRL and has led to added costs and complexity for issuers and the preparer community. When filers follow a two-tiered process whereby they prepare their interactive data as an additional step after their financial statements have been prepared to fulfill their regulatory filing needs, XBRL doesn't produce its intended results (i.e. increasing the speed and frequency with which financial information is prepared, reported, analyzed and used). Nor does it result in cost reductions.

Neither is dual filing helpful to investors. Rather, it may lead to errors and inconsistencies between the PDF and XBRL filing and cause confusion over which is the official version.

We believe the solution to this issue is the implementation of iXBRL (in-line XBRL) as it provides a means of viewing the XBRL filing itself in a human-readable, understandable and familiar format. iXBRL allows for the inclusion of XBRL tags within ordinary, human-readable XHTML documents while avoiding the need for a separate means of converting XBRL data into human-readable form.

A human-readable version of an XBRL report is useful to filers and users in ensuring the filing is accurate, consistent and complete. It also renders a separate PDF filing unnecessary.

All Aspects of Reporting

Structured reporting is most effective when it is applied broadly to all aspects of reporting — to earnings releases and all regulatory filings, such as Form 8-K, proxy statements, among others. Over time, taxonomies could be developed for the audit report, MD&A, integrated reporting etc. Indeed, such developments have taken place around the world:

• Enhanced Business Reporting Consortium (EBRC) Management Discussion & Analysis (MD&A) Taxonomy

• XBRL US Auditor Taxonomy (see US Financial Reporting – Accountants Report (USFR-AR))

• Deloitte Netherlands Annual Report in XBRL including the auditor report

First, however, structuring needs to apply to all companies. There have been discussions of smaller entities not using structured data in their filings, which prevents automated analysis of these companies for investors who invest across companies big and small. The availability of financial information in a standardized format will benefit smaller entities looking for greater interest in their companies from both institutional and retail investors.

Moreover, structured reporting is most effective when it is applied to all aspects of reporting. Tagging should cover not only the face of the annual financial statements, but also should include tagging of each note to those statements. Likewise, structured reporting should apply to all parts of the annual report, including text block tagging of the management commentary and of each significant accounting policy.

Structure reporting also should apply to all types of interim reports as investors make investment decisions at more than just year-end. Not applying the technology to interim reports brings virtually no added benefits to investors, who need a repeatable process whereby they can compare the interim and annual information in the same format (i.e. structured data)

On the basis of these reasons, we believe regulators need to require structured reporting beyond just the financial statements so that investors have the ability and the means of taking a deeper look into not just the annual reports but all supporting reports, as well.

Quality Issues

Many challenges have impeded the successful implementation of XBRL — one of the biggest being the quality of the data. Data quality issues affecting the automated analysis of XBRL data have included: inconsistent data modeling, unnecessary use of extensions, and input errors.

The XBRL US Data Quality Committee (DQC) — in which we participate — focuses on data quality issues that adversely affect data consumption and analysis by users and prioritizes issues based on input from them. We are responsible for developing guidance and validation rules that can prevent or detect inconsistencies or errors in XBRL data filed with the SEC.

We have determined that chief amongst the data quality issues that need to be addressed is the use of extensions. We — the Committee, as well as CFA Institute — believe in a structured approach to the use of extensions. Our CFA Institute publication, *eXtensible Business Reporting Language: A Guide for Investors*, states:

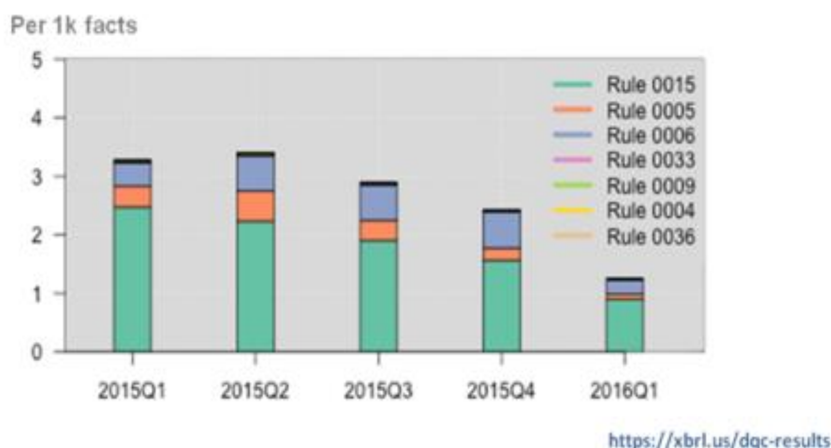
> *Individual extensions should be limited to those rare situations in which an item unique to that firm exists and the information about it does not fit into any of the concepts within the standard taxonomy or extension. We strongly encourage reporting companies to look first for the appropriate tag within the existing taxonomy before turning to a custom extension. If such a tag does not exist, we believe an extension should be allowed but within a well-defined framework so that no extension corrupts other financial statement relationships. Simply put, the automated relationships required by the computer remain:*

When a custom tag is inserted, the relationships remain intact and the numbers continue to sum up correctly.

The Committee plans to provide guidance for the appropriate use of extensions. The challenge in developing such guidance will be balancing the need for both comparability between companies and transparency in that companies need to tell their story.

The DQC conducted an analysis recently to measure the effectiveness of its first set of validation rules — which enabled validation of more than 1.9 million data points in the first quarter of 2016. The rules identify potential errors, such as incorrect negative values and incorrect dates that impede the automated analysis of data. The results are impressive. Errors for all SEC filers were reduced by 64% for the data covered by the rules (as the following chart shows).

Rule Results per Quarter, All Rules and All Filers



We are heartened by these results as they indicate a significant improvement in the quality of the data, of the reporting, and the technology itself. Consequently, we believe, and will encourage more companies to follow the DQC's validation rules, which are freely available at XBRL's website.

EDGAR

CFA Institute applauds the SEC for its ongoing efforts to enhance the functionality of the EDGAR system. The current limited search functionality leads some users to pay third-party vendors for such information. A more robust search function would make disclosure documents more accessible to a wider range of investors and better enable them to analyze registrants and make comparisons between them.

Presentation

With regard to the presentation of information we make the following points:

- We support greater use of cross-referencing to eliminate redundancies so long as the level of auditor assurance is not diminished.

- Some of the SEC's guidance limiting the use of cross-referencing pre-date the expanded use of technology that allows registrants to hyperlink. In light of technological changes, the SEC should reconsider those rules and seek to provide investors with information in a single location.
- The Release states "The Commission's rationale for limiting the use of hyperlinks was that readers might be unable to understand the content of the filing without accessing numerous hyperlinks and that readers would be unable to print the filing as an integrated whole." This assumes a paper-based system where investors print out a filing to read it and ignores how investors use technology to search through a document for information they seek.
- We support a layered approach for disclosure that permits issuers to provide summary information upfront about the key elements of disclosure within a document with the details presented later.
- With regard to the placement or presentation of registrant disclosures to facilitate identification of current, material information, we support the concept of a "company profile" or "company tab" that contains core data about the business and management of a company. This would allow investors to focus on new information about the latest fiscal period.
- We also support the increased use of tables and charts as it would be very important to improving financial reporting. Investors want quantitative tables appropriately disaggregated. Standardization of quantitative disclosures would enhance comparability over time and among firms. The quantitative information should be supported by qualitative explanations that need to be entity-specific instead of being littered with boilerplate or generic language.

Conclusion

Should you have any questions about our positions, please do not hesitate to contact Kurt N. Schacht, CFA at kurt.schacht@cfainstitute.org, 212.756.7728 or James C. Allen, CFA at james.allen@cfainstitute.org, 434.951.5558.

Sincerely,

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