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SEC Approves Rule Requiring Public Companies to Disclose Human Capital Resources

On August 26, 2020, by a 3 to 2 vote, the Securities and Exchange Commission ("SEC") adopted a final rule that would amend Regulation S-K and require public companies to disclose information on their human capital resources to the extent such disclosures would be material to an understanding of the companies' business.

Generally, a public company is required to include a description of their business and business developments in its annual report (Form 10-K) and certain other SEC filings. The disclosure rules set forth a non-exhaustive list of topics that a company should cover to the extent they are material to understanding the company's business. The new rule adopted by the SEC expands this list of topics to include a description of a company's human capital resources, including any human capital measures or objectives that a company focuses on in managing its business. The final rule identifies human capital measures or objectives that address the development, attraction and retention of personnel, as a non-exclusive example of subjects that may be material, depending on the nature of the company's business and workforce.

Notably, the SEC rejected many commenters' suggestions that the new rule should be prescriptive in nature and include a detailed list of human capital disclosures (e.g., the number of employees, and the number of full-time, part-time, seasonal, and temporary workers). Instead, and consistent with its general approach to drafting disclosure rules, the SEC chose a **principles-based and materiality-based approach** to provide public companies the flexibility to identify and disclose human capital resources and measures that are relevant to their respective businesses and specific facts and circumstances.

The new rule will be effective 30 days after publication in the Federal Register.

Meridian comment. The SEC's expanded disclosure requirements reflect the heightened focus on ESG matters by investors and other stakeholders. While some companies have included sustainability reports on their website or covered human capital considerations in their annual proxy statement, these new rules will require many companies to disclose more information on human capital matters in Form 10-K filings.

SEC Chairman Clayton noted that the final rule (and the package of other rules adopted by the SEC on August 22, 2020) "build on our materiality-based disclosure framework. The effectiveness of this framework in providing the public with the information necessary to make informed investment decisions has proven its merit time and again as markets have evolved when we have faced unanticipated events."

In its release to the final rule, the SEC noted that the Commission "did not include more prescriptive requirements because … the exact measures and objectives included in human capital management disclosure may evolve over time and may depend, and vary significantly, based on [numerous] factors, including the registrant's industry, the various regions or jurisdictions in which the registrant operates and the strategic posture of the registrant."

However, the two dissenting Commissioners believe the final rule is deficient. Specifically, Commissioner Lee noted that the final rule "leans too heavily on principles-based disclosure" and fails to cover climate change and diversity. Further, Commissioner Lee supports the development of "standardized, consistent, reliable, and comparable ESG disclosures … [that investors need] to protect their investments and allocate capital toward a sustainable economy."

Commissioner Lee may have provided a preview of future rulemaking if and when a Democratic administration appoints the SEC Chair and majority of commissioners.

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The ***Client Update*** is prepared by Meridian Compensation Partners' Technical Team led by Donald Kalfen. Questions regarding this Client Update or executive compensation technical issues may be directed to Donald Kalfen at 847-235-3605 or dkalfen@meridiancp.com.