Paul|Weiss

Client Memorandum

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2020 Year-End U.S. Legal & Regulatory Developments

In This Issue:

- **Recent Developments (Fourth Quarter 2020)**
  1. Nasdaq Proposes Board Diversity Requirements for Listed Companies
  2. SEC Adopts Final Disclosure Rules for Resource Extraction Issuers
  3. Delaware Court of Chancery Permits Buyer to Terminate Merger Due to Target's Failure to Operate in the Ordinary Course; But Finds No MAE Due to COVID-19
  4. SEC Updates Form 20-F and Form 40-F MD&A and Other Financial Disclosure Requirements
  5. SEC Updates Rules on Auditor Independence
  6. SEC Proposes Amendments to Rule 144
  7. SEC Proposes Amendments to Rule 701 and Form S-8
  8. SEC Again Approves NYSE Rule and Institutes Proceedings on Nasdaq Proposal Regarding Primary Direct Floor Listings
  9. SEC Permits Electronic Signatures
- **2020 Developments (First through Third Quarters)**
  1. SEC Adopts Simplified Disclosure Requirements for Guaranteed and Secured Notes in Registered Offerings
  2. SEC Enforcement Co-Directors Issue Statement on Potential Insider Trading and Selective Disclosure Risks Related to COVID-19
  3. SEC Adopts Amendments to Streamline Disclosures Relating to Acquisitions and Dispositions
  4. Supreme Court Upholds the SEC's Authority to Seek Disgorgement in Civil Actions, But Imposes Important Limiting Principles
  5. SEC Adopts Final Rules on Proxy Voting Advice and Related Guidance on Investment Adviser Voting Responsibilities
  6. SEC Amends Definitions of Accredited Investor and Qualified Institutional Buyer
  7. CFIUS Releases Final Regulations Changing Mandatory Filing Requirements

The following is our summary of significant 2020 U.S. legal and regulatory developments of interest to Canadian companies and their advisors. The first section below covers key developments from the fourth quarter of 2020; the second section discusses certain key developments from the first three quarters of 2020.

Recent Developments (Fourth Quarter 2020)

1. Nasdaq Proposes Board Diversity Requirements for Listed Companies

On December 1, 2020, Nasdaq proposed board diversity and disclosure requirements as a condition to continued listing. The proposed rule changes, which are subject to public comment and approval by the U.S. Securities and Exchange Commission (the "SEC"), would create new Rule 5605(f), Diverse Board Representation, and new Rule 5606, Board Diversity Disclosure, which together would prescribe a standardized format for companies to provide required statistical disclosures regarding the self-identified diversity of its board members and adopt a "comply or disclose" approach to encourage greater board diversity.

Statistical Board Diversity Disclosure

Within one year of SEC approval of the proposed listing requirements, Nasdaq would require disclosure of statistical board diversity data. After the first year, companies would need to present this statistical diversity disclosure for both the current and immediately prior year. Companies would be required to include the statistical diversity disclosure in their proxy statement or information statement for their annual meeting, or on their website. If a company elects to post the disclosure on its website, it would also need to submit the disclosures, with a URL, to the Nasdaq Listing Center within 15 calendar days after its annual shareholder meeting.

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Board Diversity Requirements

The proposed Nasdaq rules would require each listed company to have at least one female director and one director that self-identifies as an "underrepresented minority" or as LGBTQ+, or explain why it does not meet these board diversity requirements, as a condition to continued listing.

Companies would need to have at least one diverse director within two years of the SEC approval of the listing requirements, and fully comply with these requirements within four years (if listed on the Nasdaq Global Select or Global Markets) or five years (if listed on the Nasdaq Capital Market). Newly listed companies would be required to satisfy the applicable requirements within one year of listing.

If the statistical diversity disclosures reflect that a company is not in compliance with applicable board diversity requirements, that company would need to include additional disclosure (i) specifying the applicable requirements and (ii) explaining why it has not complied with them. The explanatory statement would need to be included in the company's proxy statement or information statement for its annual meeting, or on its website. Foreign private issuers would rely on website postings as they are not subject to the SEC proxy rules.

If a company fails to provide the required diversity disclosures, Nasdaq would notify the company of its noncompliance. Companies would have 45 days to submit a plan to Nasdaq to regain compliance, after which Nasdaq could allow the company up to 180 days to regain compliance. If a company failed to regain compliance, Nasdaq would issue a Staff Delisting Determination.

Foreign Issuers

The board diversity and disclosure requirements will also apply to foreign issuers, which include foreign private issuers and other foreign companies that have their principal executive offices located outside the United States. However, foreign issuers may use a different disclosure matrix reflecting the total number of directors on the board and any voluntary diversity self-identification offered by directors, provide and use an alternate definition of "underrepresented minority," based on the relevant national, racial, ethnic, indigenous, cultural, religious or linguistic identities in their home country jurisdiction; or satisfy the board diversity requirement by having two female directors.

Issuers that elect to follow an alternative diversity objective in accordance with home country practices, or are located in jurisdictions that restrict the collection of personal data, may satisfy the proposed listing requirements by explaining their reasons for doing so instead of meeting the diversity objectives of the rule.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980655/nasdaq_proposes_board_diversity_requirements_for_listed_companies.pdf

For the full text of Nasdaq's proposed rule change, please see:

- https://listingcenter.nasdaq.com/assets/RuleBook/Nasdaq/filings/SR-NASDAQ-2020-081.pdf

2. SEC Adopts Final Disclosure Rules for Resource Extraction Issuers

On December 16, 2020, the SEC adopted final disclosure rules that will require resource extraction issuers to disclose payments made to the U.S. federal government or foreign governments for the commercial development of oil, natural gas or minerals. The rule applies to SEC-reporting domestic issuers as well as foreign private issuers.

The SEC simultaneously issued an order permitting domestic and foreign private issuers to provide, in lieu of disclosure mandated by the final rules, resource extraction payment disclosures already required of them under: (i) Canada's Extractive Sector Transparency Measures (ESTMA); (ii) the EU Accounting Directive 2013/34/EU; (iii) the EU Transparency Directive 2013/50/EU; (iv) the UK Reports on Payment to Governments Regulation 2014; or (v) the Norwegian Regulation on Country-by-Country Reporting.

The final rules will become effective 60 days after the date of publication in the Federal Register. A resource extraction issuer will be required to comply with the new annual reporting requirement starting with its fiscal year ending no earlier than two years after the effective date of the final rules. Following the two-year transition period, Form SD will be due no later than 270 days after the end of an issuer's most recently completed fiscal year.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980685/sec_adopts_final_disclosure_rules_for_resource_extraction_issuers.pdf

For the SEC adopting release, please see:

- https://www.sec.gov/rules/final/2020/34-90679.pdf

For the SEC order, please see:

- https://www.sec.gov/rules/other/2020/34-90680.pdf

3. Delaware Court of Chancery Permits Buyer to Terminate Merger Due to Target's Failure to Operate in the Ordinary Course; But Finds No MAE Due to COVID-19

On November 30, 2020, the Delaware Court of Chancery in *AB Stable VIII LLC* v. *MAPS Hotels and Resorts One LLC, et al.* ("AB Stable") held that the COVID-19 pandemic did not result in a Material Adverse Effect (an "MAE") on the target because pandemics fall within the plain meaning of the MAE's exception for "natural disasters and calamities." The court found support for this conclusion in the plain meaning of the term "calamities" and the generally seller-friendly nature and allocation of systematic risk to the buyer in the MAE definition in the sale agreement.

Nevertheless, the buyer was excused from its obligation to close the transaction, and was ultimately justified in terminating the sale agreement because the target had made significant changes to its business post-signing as a result of the COVID-19 pandemic and therefore violated its covenant to operate its business in the ordinary course consistent with past practices.

In September 2019, an affiliate of Mirae Asset Financial Group (the "Buyer") agreed to acquire from the seller, an affiliate of a Chinese insurance and financial services conglomerate (the "Seller"), a luxury hotel business (the "Target"). Post-signing, due to the COVID-19 pandemic, the Target temporarily closed two of its hotels due to very low demand and governmental orders, operated its other hotels with significantly reduced staff and amenities and paused all non-essential capital spending. On the scheduled closing date in April 2020, the Buyer asserted that it was not obligated to close because the Seller had made a number of inaccurate representations and warranties and failed to comply with covenants under the relevant sale agreement and that it could terminate the agreement if the breaches remained uncured.

Although the court, in an opinion by Vice Chancellor J. Travis Laster, acknowledged that these changes were "reasonable responses to the pandemic," precedent and the language of the ordinary course covenant required the court to evaluate the Target's actions exclusively based on how it had operated in the past, and not whether they were reasonable in view of the pandemic. According to the court, management cannot "take extraordinary actions and claim that they are ordinary under the circumstances."

The phrasing of the ordinary course covenant—that it conduct its business "***only*** in the ordinary course of business, ***consistent with past practices***" (emphasis added)—created a standard that looked exclusively at how the Target has operated in the past. The court suggested that excluding the phrase "consistent with past practices" would have permitted it also to examine practices at comparable companies to determine what constituted "ordinary course."

Some key takeaways from the ***AB Stable*** opinion follow.

- Delaware courts generally operate from the baseline assumption that business risk is allocated to the seller and systematic risk to the buyer. Thus, deviation from this assumption should be clear. Similarly,

the lack of common aspects of an MAE provision could be interpreted by the court as indicative of intentional risk allocation by the parties.

- When interpreting MAE provisions, Delaware courts will default to a term's plain meaning, which could result in a broader interpretation of the term.
- In discussing ordinary course covenants, the ***AB Stable*** court did not address whether contracts entered into after the COVID-19 pandemic began should be interpreted so that "ordinary course consistent with past practice" includes actions taken during the pandemic. Parties should consider whether extraordinary, pandemic-related actions are "ordinary course" and draft their agreements accordingly.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980662/delaware_court_of_chancery_permits_buyer_to_terminate_merger_due_to_target-s_failure_to_operate_in_the_ordinary_course_but_finds_no_mae_due_to_covid-19.pdf

For the full text of the opinion, please see:

- https://courts.delaware.gov/Opinions/Download.aspx?id=313600

4. SEC Updates Form 20-F and Form 40-F MD&A and Other Financial Disclosure Requirements

On November 19, 2020, the SEC adopted amendments to the financial disclosure requirements of Regulation S-K, including the requirements, set out in Item 303, governing the presentation of Management's Discussion and Analysis (the "MD&A"). These amendments are a part of the SEC's modernization initiatives, and are intended to better focus disclosure on material information while reducing compliance efforts for SEC reporting companies. The amendments introduce a more principles-based approach to MD&A, reducing duplicative disclosures and codifying certain SEC guidance.

The MD&A amendments include the addition of a new introductory section to MD&A intended to help registrants focus on the key purpose of MD&A and on "material" and "reasonably likely" impacts. This section codifies guidance that registrants should provide a narrative explanation of their financial statements that would enable investors to see the registrant "through the eyes of management."

- *Objective*: This is a new introductory section to MD&A, and is intended to help companies focus on the key purpose of MD&A and on "material" and "reasonably likely" impacts.

- *Liquidity and Capital Resources*: These disclosure items have been combined and updated to require disclosure of "material cash requirements."

- *Critical Accounting Estimates*: The amendments codify and enhance prior SEC guidance to require the disclosure and discussion of critical accounting estimates.

- *Off-Balance Sheet Arrangements and Tabular Disclosure of Contractual Obligations*: As part of the effort to reduce duplicative disclosure, current Items 303(a)(4) (off-balance sheet arrangements) and 303(a)(5) (tabular disclosure of contractual obligations), both introduced in 2003 as part of the Sarbanes-Oxley reforms, have been eliminated.

- *Interim Period Disclosures*: The amendments give companies the flexibility to compare quarterly results to the prior year's quarter or the immediately preceding quarter.

In addition, the amendments eliminate the requirement to present five years of selected financial data (Item 301), and simplify and streamline the presentation of supplementary financial data (Item 302). Companies will no longer be required to provide two years of tabular supplementary quarterly financial information.

The SEC made several conforming changes to Form 20-F and Form 40-F to ensure that the existing MD&A requirements for foreign private issuers mirror these changes.

Form 20-F

The amendments eliminate current Item 3.A of Form 20-F, which requires foreign private issuers to disclose selected financial data for the most recent five fiscal years. The required trend disclosure will instead be provided in response to Item 5 of Form 20-F.

In order to align Item 5 of Form 20-F with the revised Item 303 of Regulation S-K, the amendments specify that Item 5 disclosure should include, among other things, statistical data that will improve a reader's understanding of the registrant's financial condition, changes in financial condition and results of operations, quantitative and qualitative description of the reasons underlying material changes, including where material changes within a line item offset each other, and information relating to the registrant's other subdivisions, such as geographic areas or product lines.

The amendments also added new principles-based disclosure requirements regarding liquidity and capital resources disclosures and off-balance sheet arrangements to Item 5. The amendments modified 5.A.2 to require only the disclosure of the impact of hyperinflation if hyperinflation has occurred in any of the periods for which audited financial statements or unaudited financial statements are filed, amended Item 5.D to require foreign private issuers to disclose "material trends" instead of "the most significant recent

trends" and modified Item 5.E to explicitly require disclosure of critical accounting estimates to the extent reasonably available and material.

Form 40-F

The amendments also revise Form 40-F to align it with revised Item 303 of Regulation S-K, including replacing the contractual obligations and off-balance sheet arrangements disclosure requirements with principles-based instructions that require, to the extent it is not already provided in the MD&A required under Canadian law, an analysis of material cash requirements from known contractual and other obligations and a discussion of off-balance sheet arrangements that have or are reasonably likely to have a material current or future effect on the registrant's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, cash requirements or capital resources.

The amendments will be effective February 10, 2021. Registrants will be required to apply the amended rules for the first fiscal year ending on or after August 9, 2021, and will be required to apply the amended rules in registration statements and prospectuses that at the time of the initial filing are required to contain financial statements for a period on or after August 9, 2021. Registrants may comply with the amended requirements at any time after the effective date, so long as they comply with any amended item in its entirety.

For the full text of our memorandum describing the amendments to Regulation S-K, please see:

- https://www.paulweiss.com/media/3980631/sec_updates_mda_and_other_financial_disclosure_requirements.pdf

For the full text of our memorandum describing the changes to Form 20-F and Form 40-F, please see:

- https://www.paulweiss.com/media/3980632/sec_updates_form_20-f_and_form_40-f_mda_and_other_financial_disclosure_requirements.pdf

For the SEC adopting release, please see:

- https://www.sec.gov/rules/final/2020/33-10890.pdf

5. SEC Updates Rules on Auditor Independence

On October 16, 2020, the SEC adopted amendments to certain auditor independence requirements set forth in Regulation S-X. Under the amendments, certain relationships and services that previously would have run afoul of the independence requirements, and that the SEC believes do not impair the objectivity or impartiality of auditors, will be permitted.

Key changes include harmonizing the look-back period for the "audit and professional engagement period" for first-time filers, amending the business relationship rule (Rule 2-01(c)(3)) to focus the analysis on those associated persons with decision-making capacity over the entity under audit and adopting a framework (in revised Rule 2-01(e)) to allow audit firms and their clients to transition out of services or relationships that, due to a pending merger or acquisition, will no longer meet the independence standards.

The amendments will become effective June 9, 2021. Auditors may choose to voluntarily comply with the amendments at any time after December 11, 2020, provided that if they do so, the final amendments must be applied in their entirety from the date of such early compliance.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980551/sec_updates_rules_on_auditor_independence.pdf

For the SEC adopting release, please see:

- https://www.sec.gov/rules/final/2020/33-10876.pdf

6. SEC Proposes Amendments to Rule 144

On December 22, 2020, the SEC proposed amendments to Rule 144 ("Rule 144") under the U.S. Securities Act of 1933, as amended (the "Securities Act"), which sets forth a non-exclusive safe harbor from registration for resales of restricted and control securities.

Under the proposal, electronic filing of Form 144 would be mandatory with respect to securities issued by issuers subject to reporting requirements under the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"). Additional copies of the Form 144 would no longer need to be mailed to the principal exchange on which the securities trade. The Form 144 would be required to be filed by the end of the second business day following the day of the transaction to coincide with the Form 4 deadline, whether or not a Form 4 would be required to report the transaction.

In addition, the SEC has proposed certain amendments to streamline the EDGAR filing process where both a Form 144 and a Form 4 are required to report the same transaction. Filers would need to input the filing information only once into the EDGAR system, which could then generate both a Form 144 and a Form 4.

Under the proposed amendments, Form 144 would no longer be required to be filed in respect of securities of issuers that are not subject to Exchange Act reporting requirements. This proposed revision would not alter any other conditions that would otherwise need to be met in order for resales of securities of non-reporting issuers to qualify for the Rule 144 safe harbor.

Historically, in the case of convertible securities, Rule 144 has permitted a holder to tack the holding period of the convertible instrument and the underlying security, where the underlying security is acquired solely in exchange for the convertible instrument. Under proposed amendments, the holding period for securities acquired upon the conversion or exchange of certain market-adjustable securities would not begin until the securities are acquired upon conversion or exchange where the convertible or exchangeable security contains terms that offset, in whole or in part, declines in the market value of the underlying securities occurring prior to conversion or exchange, other than terms that adjust for stock splits, dividends or other issuer-initiated changes in its capitalization and where the issuer does not have a class of securities listed on a national securities exchange.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980704/sec_proposes_amendments_to_rule_144.pdf

For the SEC proposed rule change, please see:

- https://www.sec.gov/rules/proposed/2020/33-10911.pdf

7. SEC Proposes Amendments to Rule 701 and Form S-8

On November 24, 2020, the SEC proposed amendments to modernize the securities law framework for equity compensation offerings to employees and other service providers. These amendments would benefit both domestic issuers and foreign private issuers, and certain of the proposed amendments are for the specific benefit of foreign private issuers. The SEC has requested comments on the proposal on or before February 9, 2021.

The proposed amendments would expand the eligible recipients of securities issued under Rule 701 of the Securities Act ("Rule 701") and Form S-8 to include, subject to certain conditions, consultants and advisors that are entities, former employees, with respect to post-termination grants in connection with prior employment or service, former employees of acquired entities, with respect to the acquiring company securities issued in exchange or substitution for the acquired entity's securities, and employees of any subsidiary.

The proposed amendments to Rule 701 would increase two of the three calculations for the maximum amount of securities issuable pursuant to Rule 701, so that issuers could, in any 12-month period, sell securities in an amount up to the greater of 25% of assets (up from 15%), $2 million (up from $1 million) or 15% of the amount or class of securities offered (unchanged). In the case of completed business combination transactions, the acquiring issuer would be able to use a pro forma balance sheet that reflects the transaction or a balance sheet as of a date after the completion of the transaction that reflects the total assets and outstanding securities of the combined entity.

Additionally, the proposed changes would relax the disclosure requirements for issuances under Rule 701 exceeding $10 million in any 12-month period by requiring these disclosures only for issuances in excess of the $10 million threshold rather than with respect to all issuances, including those made before the $10 million threshold is surpassed. Issuers would also only need to prepare the required financial statements semi-annually instead of quarterly. This requirement has proved particularly burdensome for foreign private issuers that are normally required to provide only semi-annual and annual financial statements under their home country rules.

Under the proposed amendments, foreign private issuers that are eligible for the exemption from Exchange Act registration under Rule 12g3-2(b) would be permitted to provide financial statements prepared in accordance with home country accounting standards for purposes of Rule 701(e) disclosure without reconciliation to U.S. GAAP if financial statements prepared in accordance with U.S. GAAP or IFRS are not otherwise available.

Furthermore, the proposed amendments to Form S-8 would clarify that issuers may use an automatically effective post-effective amendment to an existing Form S-8 to add plans, additional securities and additional classes of securities, instead of filing a new Form S-8, and may use a single Form S-8 to register an unallocated pool of securities underlying multiple incentive plans.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980650/sec_proposes_amendments_to_rule_701_and_form_s-8____.pdf

For the SEC proposed rule change, please see:

- https://www.sec.gov/rules/proposed/2020/33-10891.pdf

8. SEC Again Approves NYSE Rule and Institutes Proceedings on Nasdaq Proposal Regarding Primary Direct Floor Listings

On December 22, 2020, the SEC again approved the NYSE's proposed rule change to permit primary direct floor listings. This approval comes at the conclusion of the SEC's de novo review of the NYSE's proposal in response to a petition to review filed by the Council of Institutional Investors on September 8, 2020, after the SEC's initial approval of the proposal on August 26, 2020. This approval follows the SEC's December 17, 2020 order instituting proceedings to determine whether to approve or disapprove Nasdaq's proposed rule change to permit direct floor listings. As it did with the NYSE proposal, the Council of Institutional Investors has urged the SEC to disapprove the Nasdaq proposal.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980700/update_on_primary_direct_floor_listings_sec_again_approves_nyse_rule_and_institutes_proceedings_on_nasdaq_proposal.pdf

For the SEC release approving the proposed rule change, please see:

- https://www.sec.gov/rules/other/2020/34-90768.pdf

9. SEC Permits Electronic Signatures

On November 17, 2020, as part of its modernization efforts, the SEC adopted amendments to allow for electronic signature of documents filed with the SEC via EDGAR. The SEC has also revised rules and forms under the Securities Act, Exchange Act and Investment Company Act of 1940 to allow the use of electronic signatures for other filings that contain typed, rather than manual, signatures. The amendments became effective on December 4, 2020.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980616/sec_to_permit_electronic_signatures.pdf

For the SEC adopting release, please see:

- https://www.sec.gov/rules/final/2020/33-10889.pdf

2020 Developments (First through Third Quarters)

1. SEC Adopts Simplified Disclosure Requirements for Guaranteed and Secured Notes in Registered Offerings

On March 2, 2020, the SEC published final rules amending and simplifying the financial disclosure requirements of Rule 3-10 of Regulation S-X for issuers and guarantors of registered guaranteed debt securities and of Rule 3-16 of Regulation S-X for affiliates whose securities collateralize registered securities issued by their affiliated issuers. Rules 3-10 and 3-16 are based on an overarching principle that purchasers of guaranteed debt securities make their investment decisions by relying primarily on the consolidated financial statements of the parent company registrant and supplemental details about the consolidated subsidiary issuers and guarantors. In that context, the goal of the revised rules is to improve the quality of disclosure and encourage registrants to conduct debt offerings on a registered basis by focusing on material information that is relevant to investors and eliminating prescriptive requirements that are unnecessary and burdensome.

The final rules reflect revisions to existing Rule 3-10 and to Rule 3-16 (which remains in place for transitional purposes) and the creation of two new rules, Rule 13-01 (corresponding to Rule 3-10) and 13-02 (corresponding to Rule 3-16). The new rules now comprise new Article 13. The final rules became effective January 4, 2021.

Rule 3-10 Amendments and New Rule 13-01

Previously, Rule 3-10 required registrants to file separate annual audited and unaudited interim financial statements for each issuer and guarantor of their registered debt securities, unless one of five exceptions applies. Revised Rule 3-10 continues to permit registrants to omit separate financial statements of subsidiary issuers and/or guarantors if a prescribed set of eligibility criteria is met and the parent company provides, to the extent material, certain supplemental financial and non-financial disclosure about the subsidiary issuers and/or guarantors and the guarantees. Revised Rule 3-10 also simplifies the existing disclosure requirements, including by: replacing the requirement for condensed consolidating financial information with a requirement for certain new financial and non-financial disclosures; excluding non-issuer and non-guarantor subsidiary information; and reducing the length of time during which the parent company is required to provide supplemental financial and non-financial information.

Rule 3-16 Amendments and New Rule 13-02

Rule 3-16 previously required a registrant to provide separate annual and interim financial statements for each affiliate whose securities constitute a "substantial portion" of the collateral for the securities registered or being registered, as if the affiliate were the registrant itself. Under revised Rule 3-16, the existing requirement to provide separate financial statements of an affiliate is replaced with a new requirement that the registrant provide financial and non-financial information about the affiliate and the collateral arrangement as a supplement to the registrant's consolidated financial statements. Revised Rule 3-16 also eliminates the "substantial portion" test and requires the specified financial and non-financial disclosures in all cases unless they are not material to holders of the collateralized security. It also requires disclosure of any additional information about the collateral arrangement and each affiliate whose security is pledged as collateral that would be material to making an investment decision with respect to the collateralized security.

New Rule 13-02(a)(1)-(7)[2] specifies in more detail the financial and non-financial information required to be provided in relation to affiliates whose securities collateralize securities registered or being registered, and provides the registrant with the flexibility to place these financial and non-financial disclosures about affiliates either in a footnote to its consolidated financial statements or, alternatively, in the MD&A or in its prospectus.

Foreign private issuers are required to fully comply with revised Rule 3-10, Rule 13-01 and Rule 13-02. A foreign private issuer that prepares its financial statements on a basis other than U.S. GAAP or IFRS as

issued by the International Accounting Standards Board is not required to reconcile the supplemental financial disclosures required by Rule 3-10 and Rule 13-01 to U.S. GAAP.

We note that while revised Rule 3-10 provides significant relief from the current guarantor footnote requirement, the Rule 144A market is comfortable with even less information—a few line items of non-guarantor information—and, as such, it is likely that the Rule 144A market will continue to carve out Rule 3-10 information from expected disclosures. At the same time, the revised Rule 3-16 requirements could result in collateral being carved back in under existing debt agreements and could result in additional disclosure requirements.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3979446/17mar20-sec-client-alert.pdf

For the SEC adopting release, please see:

- https://www.sec.gov/rules/final/2020/33-10762.pdf

2. SEC Enforcement Co-Directors Issue Statement on Potential Insider Trading and Selective Disclosure Risks Related to COVID-19

On March 23, 2020, SEC Division of Enforcement Co-Directors Stephanie Avakian and Steven Peikin issued a statement concerning maintaining "market integrity" in light of the unprecedented and myriad impacts of the COVID-19 pandemic, and the increased likelihood that reporting company insiders could be in possession of material nonpublic information.

The Co-Directors observed that officers, directors and other corporate insiders are "regularly learning new material nonpublic information," and that such information may take on even greater value given current circumstances, especially if there is a delay in filing required SEC disclosure or earnings reports. The Co-Directors stressed the importance of companies adhering to corporate controls and procedures around the use and dissemination of material nonpublic information, including their disclosure controls and procedures, insider trading prohibitions, codes of ethics and Regulation FD procedures. The SEC's statement also urged broker-dealers, investment advisers and other registrants to be mindful of the need to continue complying with policies and procedures designed to prevent the misuse of material nonpublic information.

Given volatility in the market, and the potentially heightened importance and wider dissemination of material nonpublic information, public companies, their advisors and other market participants should be especially mindful of the risks of using or selectively disclosing material nonpublic information and continue to strictly enforce relevant controls and procedures. In addition, given the sharp rise in the number

of people now working remotely, companies may wish to remind employees of the need to safeguard and properly handle confidential information, including but not limited to material nonpublic information, while they are outside the physical confines of the office.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3979664/25mar20-sec-enforcement-co-directors-statement.pdf

For the SEC Enforcement Co-Directors' statement, please see:

- https://www.sec.gov/news/public-statement/statement-enforcement-co-directors-market-integrity

3. SEC Adopts Amendments to Streamline Disclosures Relating to Acquisitions and Dispositions

On May 20, 2020, the SEC adopted final rules amending Regulation S-X to streamline the information that SEC registrants must disclose in connection with significant acquisitions of other businesses as well as dispositions. The amendments affect both the financial statements that must be presented for significant acquired and to be acquired businesses as well as pro forma financial information reflecting such acquisitions, or significant dispositions.

The final rules, which became effective on January 1, 2021, amend portions of Rule 3-05, Rule 3-14 and Article 11 of Regulation S-X, make corresponding changes to the smaller reporting company requirements in Article 8 of Regulation S-X and introduce new Rule 6-11 of Regulation S-X that covers financial reporting in the event of a fund acquisition by an investment company. Among other things, the final rules: update the significance tests; limit the financial statement requirement to a maximum of two years; permit abbreviated financial statements in certain circumstances; clarify when financial statements and pro forma information are required; permit the use of International Financial Reporting Standards; no longer require separate acquired business financial statements after nine months/one year; expand the use of pro forma financial information for significance testing; amend pro forma financial information requirements to improve its relevance; and revise significance threshold for the disposition of a business.

The changes to Regulation S-X are part of a disclosure simplification process that has been ongoing for a few years. These changes, while highly technical, will greatly ease some of the more significant burdens associated with presenting financial statements and pro forma financial information in connection with acquisitions by SEC reporting companies.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980221/27may20-sec-finalizes-rules-to-streamline-disclosures.pdf

For the SEC adopting release, please see:

- https://www.sec.gov/rules/final/2020/33-10786.pdf

4. Supreme Court Upholds the SEC's Authority to Seek Disgorgement in Civil Actions, But Imposes Important Limiting Principles

On June 22, 2020, in its decision in *Liu* v. *Securities & Exchange Commission*, the Supreme Court held that the SEC may seek disgorgement in enforcement actions pursuant to its statutory authority under 15 U.S.C. § 78u(d)(5) to obtain equitable relief. In an earlier decision, *Kokesh* v. *Securities & Exchange Commission*, the Supreme Court had characterized disgorgement as a "penalty" under the general federal statute of limitation applicable to the enforcement of penalties. *Kokesh* had arguably called into question whether disgorgement constitutes equitable relief for purposes of the SEC's statutory authority, and thus set the stage for *Liu*. *Kokesh* and *Liu* were discussed in depth in our June 6, 2017 and November 4, 2019 client alerts, hyperlinked below.

In *Liu*, the Supreme Court upheld courts' equitable authority to award disgorgement in SEC enforcement actions, but held that to be valid, the awards should adhere to the following principles: (1) the amount disgorged must not exceed the wrongdoer's net profits; (2) the disgorgement must be obtained for the benefit of investors; and (3) a disgorgement order against affiliates may be unjust depending on certain enumerated circumstances. The Court's decision provides welcome guidance in an area where there previously was a limited basis for challenging the discretion of the SEC, and provides potential defendants in SEC enforcement proceedings with clear grounds for resisting unreasonable disgorgement demands.

However, the Supreme Court left open certain questions. Though the Court distinguished between "legitimate expenses," which may be deducted from a disgorgement remedy, and "inequitable deductions such as for personal services," the Court did not address how a district court might distinguish between the two, nor did the Court address which party has the burden of proving whether expenses should be excluded from a disgorgement award. Furthermore, the Court's pronouncement that any disgorgement should generally benefit victims also left open certain questions, including whether and in what circumstances the decision to deposit disgorged funds in the Treasury would benefit victims of the fraud, as required by statute and equitable principles. It is not clear how this new factor will impact the SEC's efforts to seek disgorgement, and the SEC may issue further guidance as a result.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980335/25june20-liu-v-sec.pdf

For the full text of the Supreme Court decision, please see:

- https://www.supremecourt.gov/opinions/19pdf/18-1501_8n5a.pdf

For our June 6, 2017 memorandum on *Kokesh*, please see:

- https://www.paulweiss.com/media/3977137/6june17-kokesh.pdf

For our November 4, 2019 memorandum on *Liu*, please see:

- https://www.paulweiss.com/media/3979109/4nov19-liu-v-sec.pdf

5. SEC Adopts Final Rules on Proxy Voting Advice and Related Guidance on Investment Adviser Voting Responsibilities

On July 22, 2020, the SEC voted 3-1 to adopt final rule changes and related guidance on proxy voting advice. In a move welcomed by companies, but strongly opposed by proxy advisory firms and their investor clients, the final rules take a "principles-based" approach to the regulation of proxy voting advice.

The amendments, among other things:

- codify the SEC's longstanding view that proxy voting advice generally constitutes a solicitation for purposes of the proxy rules;
- but provide that a proxy advisory firm may avail itself of exemptions from certain information and filing requirements of the proxy rules if it:
  - provides specified conflicts of interest disclosure in its proxy voting advice or in an electronic medium used to deliver the advice (failure to disclose such conflicts and the methodologies and sources of information used could be considered materially misleading in violation of Rule 14a-9's antifraud provisions); and
  - adopts and publicly discloses written policies and procedures reasonably designed to ensure that (i) companies that are the subject of proxy voting advice have access to the advice prior to or at the time the advice is disseminated to the proxy advisory firm's clients and (ii) its clients have a mechanism by which they can reasonably expect to become aware of any written statements

regarding the proxy voting advice from companies that are the subject of such advice, in a timely manner before the applicable shareholder meeting.

Proxy advisory firms have until December 21, 2021 to implement these new procedures.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980386/22july20-sec-proxy-voting.pdf

For the SEC press release on these rule amendments, please see:

- https://www.sec.gov/news/press-release/2020-161

6. SEC Amends Definitions of Accredited Investor and Qualified Institutional Buyer

On August 26, 2020, the SEC adopted final amendments to the definitions of "accredited investor" ("AI") and "qualified institutional buyer" ("QIB") to include new AI categories of natural persons and entities and an expanded list of eligible entities that qualify as QIBs. The AI definition is used principally to determine to whom securities can be sold in private placements under Rules 506(b) and 506(c) of Regulation D, and the QIB definition is used principally to determine to whom securities can be resold under Rule 144A.

Subscription agreements used for offerings of interests in private funds, as well as investor letters and other documents distributed in connection with private placements, tend to set out in full the definitions of AI and QIB, and these documents as well as indentures, offering memorandums and securities law legends typically make specific reference to "accredited investors within the meaning of sub-paragraphs (1), (2), (3) or (7) of Rule 501(a)" when intending to cover institutional accredited investors, as there is no technical definition of "institutional accredited investor." Practitioners should consider modifying subscription agreements and other documents to reflect the changes to the AI and QIB definitions.

The amendments to the AI and QIB definitions, although modest in scope, are a welcome step towards the modernization of the two concepts that play a key role in determining investors' eligibility to participate in private securities offerings. The definitions have remained largely unchanged for over 35 years.

The amendments became effective December 8, 2020.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980449/sec_amends_definitions_of_accredited_investor_and_qualified_institutional_buyer.pdf

For the SEC adopting release, please see:

- https://www.sec.gov/rules/final/2020/33-10824.pdf

7. CFIUS Releases Final Regulations Changing Mandatory Filing Requirements

On September 11, 2020, the Treasury Department released final versions of regulatory changes to fundamentally change the requirements for Committee on Foreign Investment in the United States ("CFIUS") filings implemented under the Foreign Investment Risk Review Modernization Act of 2008 ("FIRRMA"). These changes became effective on October 15, 2020. However, the previous rules apply to any transaction where the parties signed a binding agreement prior to October 15.

Previously, a mandatory CFIUS filing was required whenever (i) a foreign person acquired control over, or made a covered investment in, a U.S. business involved with critical technologies in certain industry sectors and (ii) a covered control transaction or covered investment resulted in the acquisition of a substantial interest in a U.S. business that involves critical technology, critical infrastructure, or the maintenance or collection of sensitive personal data of U.S. citizens (a "TID U.S. business") by a foreign person in which a foreign government has a substantial interest. The mandatory filing requirements were discussed in depth in our February 27, 2020 client alert, hyperlinked below.

Under the recent regulatory changes, the focus is no longer on the industry sector to which the TID U.S. business's critical technology is linked, but rather on whether the foreign person acquiring control over, or making the covered investment in, the TID U.S. business (i) has its principal place of business in a country to which a transfer of the U.S. business's critical technology would require a U.S. export control license or (ii) has 25% or more of its voting interest controlled by another foreign person or group of foreign persons whose principal place of business (in the case of entities) or nationality (in the case of individuals) is linked to a country to which a transfer of the U.S. business's critical technology would require a U.S. export control license.

The result of this important change is to make an export control assessment critical in determining whether a mandatory CFIUS filing is triggered by a particular acquisition of control over, or a covered investment in, a TID U.S. business.

Another important consequence of this recent change is to place a heavier filing burden on countries that are the target of more stringent U.S. export controls, while investors from U.S. allies (including, e.g., Canada) will be significantly less likely to trigger a mandatory filing requirement.

An additional change with respect to the mandatory filing requirement for foreign government-linked acquisitions and covered investments is more minor in nature. The FIRRMA implementing regulations provided that, in the case of a foreign person that has a general partner, managing member or the

equivalent, the national or subnational governments of a single foreign state will be considered to have a substantial interest in that foreign person only where those governments hold 49 percent or more of the interest in the general partner, managing member or the equivalent. In the recent regulations, this provision was changed so that it would only apply to partnerships and similar entities whose activities are directed, controlled or coordinated by or on behalf of the general partner, managing member or the equivalent.

For the full text of our memorandum, please see:

- https://www.paulweiss.com/media/3980482/cfius_releases_final_regulations_changing_mandatory_filing_requirements.pdf

For our June 4, 2020 memorandum on CFIUS changes, please see:

- https://www.paulweiss.com/media/3980262/4jun20-cfius-filing-requirements.pdf

For our February 27, 2020 memorandum on the final regulations implementing FIRRMA, please see:

- https://www.paulweiss.com/media/3979361/27feb20-firrma.pdf

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For a discussion of certain other developments not highlighted above, please see our memoranda available at:

- http://www.paulweiss.com/practices/region/canada.aspx

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Matthew W. Abbott +1-212-373-3402 mabbott@paulweiss.com	Christopher J. Cummings +1-416-504-0522 ccummings@paulweiss.com	Andrew J. Foley +1-212-373-3078 afoley@paulweiss.com
Adam M. Givertz +1-416-504-0525 agivertz@paulweiss.com	Audra J. Soloway +1- 212-373-3289 asoloway@paulweiss.com	Stephen C. Centa +1-416-504-0527 scenta@paulweiss.com
Christian G. Kurtz +1-416-504-0524 ckurtz@paulweiss.com	Rosita Lee +1-212-373-3564 rlee@paulweiss.com	Andrea Quek +1-416-504-0535 aquek@paulweiss.com

Associate Thea Winterton-Perks and Law Clerk Katharine Wilson contributed to this Client Memorandum.