Revised SEC Confidential Treatment Regime for Certain Exhibits: First Analysis

A Lexis Practice Advisor® Practice Note by
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Introduction

This article discusses the Securities and Exchange Commission's (SEC's) revised procedures, adopted on March 20, 2019 and effective as of April 2, 2019, for redacting competitively sensitive information from material contracts that are filed as exhibits to certain filings under the Securities Act of 1933, as amended (the Securities Act) and the Securities Exchange Act of 1934, as amended (the Exchange Act). The SEC expects that these revisions—which are part of a broad range of other amendments and rules that have been adopted or proposed by the SEC pursuant to its mandate under the Fixing America's Surface Transportation Act of 2015 (the FAST Act) with the goal of modernizing and simplifying the public company disclosure regime—will result in significant cost reduction for reporting companies while expediting the confidential treatment process.

In order to redact competitively sensitive information from material contracts under the new rules, a company must:

- Mark the exhibit index in the applicable filing to indicate that portions of the exhibit or exhibits have been omitted;
- Include a prominent statement on the first page of the redacted exhibit that certain information has been excluded from the exhibit because it (a) is not material and (b) would likely cause competitive harm to the company if publicly disclosed and;
- Indicate with brackets where the information has been omitted from the filed version of the exhibit.

The new rules only apply to exhibits filed under Item 601(b)(10) of Regulation S-K, which covers material contracts made outside the ordinary course to be performed at or after filing, and Item 601(b)(2) of Regulation S-K, which covers agreements effecting mergers and acquisitions, reorganizations, liquidations or other similar events. The SEC has also adopted conforming changes to certain forms to which the exhibit requirements of Item 601 of Regulation S-K do not apply, including Form 8-K and Form 20-F.

For further information on disclosure obligations of public companies under the Exchange Act, see Public Company Periodic Reporting and Disclosure Obligations. For a comprehensive list of Lexis Practice Advisor resources regarding the topics covered in this article, see Periodic and Current Reporting Resource Kit.

Initial Guidance

Elimination of CTRs

The most conspicuous and welcome change implemented by the amendments is the elimination of the requirement that companies file confidential treatment requests (CTRs) with the SEC. Prior to the effectiveness of the new rules, a company wishing to redact competitively sensitive information from a material contract was required, under Securities Act Rule 406 (17 C.F.R. § 230.406) or Exchange Act Rule 24b-2 (17 C.F.R. § 240.24b-2), to submit a CTR to the SEC that:

- Established the legal and factual bases for redaction under the relevant provisions of the Freedom of Information Act (FOIA) and;
- Explained why, based on the facts and circumstances of the particular case, disclosure of the information was unnecessary for investor protection.

The preparation of CTRs and any related correspondence with the SEC's Division of Corporate Finance (the Staff) often required substantial legal analysis, which could be expensive and time-consuming. Although a CTR is still required if a company wishes to seek confidential treatment on the basis of FOIA's other exemptions (e.g., for privileged information) or with respect to exhibits that are not filed pursuant to Item 601(b)(10) or (b)(2) of Regulation S-K, the SEC estimates, based on historical data, that the amendments could reduce the number and cost of CTRs by over 90%.

Another benefit of the amendments is that, generally, redacted information will remain confidential without any time limit, because unredacted materials will not necessarily be provided to the Staff. Under the prior regime, companies were required to submit unredacted copies of the agreements with the CTRs, which were protected from public disclosure only for a period of time specified in the confidentiality order (typically no longer than 10 years). To ensure continued confidentiality beyond this time, companies were forced to monitor the expiry of, and submit requests to extend, those orders. The new rules obviate the need for such monitoring by eliminating the requirement that companies submit unredacted copies in the first instance.

Preparing for Compliance Reviews

The elimination of the CTR requirement does not provide carte blanche for expansive redactions and does not reflect a substantive change in the SEC's criteria for appropriate redactions. In the release adopting the amendments, the SEC stressed that the changes were procedural in nature and do not affect the principles of what a registrant may or may not permissibly redact from its disclosure for reasons of confidentiality.

To ensure adherence to these principles in the absence of CTRs, the Staff plans to selectively assess whether redactions in exhibits are limited to immaterial information that would hurt a company's competitive position if disclosed. That assessment would initially take the form of a request for written copies of unredacted materials, but may eventually result in a request for legal and factual substantiation of a company's redactions similar to those previously required in a CTR. Therefore, in preparing for the possibility of such requests, companies should consider maintaining the standards and controls that they had in place prior to the effectiveness of the amendments. Notably, if the Staff's review is in connection with a company's Securities Act registration statement, consistent with prior practice, the company will be expected to resolve any questions relating to redacted exhibits before submitting a request for acceleration of the effective date of the registration statement.

Only the initial request for unredacted materials and the closing-of-review letters will be available on EDGAR. Any comments from the Staff following its review of the unredacted materials and responses thereto will not be publicly available and will be kept separate from the review of other aspects of the filing. If a company's filing is selected for review, the company will need to carefully review the instructions for separate delivery in order to avoid inadvertent public disclosure. Further, in order to protect unredacted agreements from FOIA requests, companies should request confidential treatment under Rule 83 (17 C.F.R. § 200.83) while sensitive materials are under review and request the return or destruction of such materials (under Securities Act Rule 418 (17 C.F.R. § 230.418) or Exchange Act Rule 12b-4 (17 CFR 240.12b-4)) after the review is complete.

Transitioning to the New Confidentiality Regime

The SEC also provided a transition plan for companies that have pending or approved CTRs as of the date of effectiveness of the new regime. If a company has received an order granting confidential treatment that is still effective, the grant of confidential treatment will continue until the date stated on the order. Once that date has passed, however, companies cannot prevent public disclosure by refiling redacted versions of the agreements under the new rules, because the unredacted agreements already in the SEC's possession are no longer protected from FOIA requests at such time. They should instead request an extension of the original confidential treatment, consistent with practice prior to these amendments.

Looking Ahead

The extent to which companies will be scrutinized for compliance with the new rules remains to be seen. Those who opposed the amendments believe they create undue risk to investors as a result of reduced SEC oversight. For example, SEC Commissioner Robert J. Jackson Jr., who dissented to the adoption of the amendments, wrote that the new rule "removes our Staff's role as gatekeepers when companies redact information from disclosures—despite evidence that redactions *already* deprive investors of important information." In response, the SEC has emphasized its continued prerogative to scrutinize redactions through selective assessment. One data point that may be interesting to monitor will be the frequency of amendments to filings that reveal all or portions of information previously redacted. Another potential indicator will be whether the SEC expands the revised rules to cover other exhibits under Item 601(b) of Regulation S-K (such as underwriting agreements, expert opinions or organizational documents). Regardless, these amendments represent a meaningful step towards easing the burden of obtaining confidential treatment of competitively sensitive information in material contracts filed as exhibits to SEC filings.

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Mr. Arcella has been cited as a leading practitioner in securities and corporate law by *Chambers USA*, *Chambers Global*, *The Legal 500 United States*, *IFLR1000*, *The Best Lawyers in America*, *The Legal 500 Latin America* and *Latin Lawyer 250*. Mr. Arcella has also been named to *The Legal 500* Hall of Fame in the Capital Markets: Debt Offerings and Capital Markets: High-Yield Debt Offerings categories.

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