

# SEC in Focus

Quarterly summary of current SEC activities

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## SEC staff discuss priorities of its Disclosure Review Program

The staff of the Securities and Exchange Commission (SEC or Commission) recently **said** that the top areas of comment for the fiscal year ended 30 September 2023 included non-GAAP disclosures, management’s discussion and analysis (MD&A), revenue recognition, China-related matters and financial statement presentation.

Erik Gerding, Director of the SEC’s Division of Corporation Finance (DCF), and other SEC staff members highlighted recent areas of focus and current priorities of the DCF’s disclosure review program at the Practising Law Institute’s *The SEC Speaks in 2024* conference in April. The program is the SEC’s primary mechanism to monitor and enhance compliance with disclosure rules and accounting requirements in periodic filings.

Mr. Gerding also said that areas of focus in 2023 included emerging areas, such as market disruptions in the banking industry, cybersecurity risks, the impact of inflation and disclosure related to newly adopted rules, such as pay versus performance.

Mr. Gerding noted that the staff’s approach to reviewing the implementation of rules in their first year of adoption generally results in forward-looking comments and allows the staff to observe any disclosure issues for which staff guidance could be helpful. For example, the SEC staff published a number of compliance and disclosure interpretations (C&Dis) on the pay versus performance rules as a result of the staff’s review process.

Looking ahead, the SEC staff expects to continue focusing on China-based companies, inflation and market disruptions in the banking industry, as well as on financial reporting topics that involve judgment and relate to recently issued accounting standards. These areas could include cybersecurity, segment reporting, non-GAAP compliance, clawbacks, critical accounting estimates and disclosures on supplier finance programs.



In addition, new priorities of the DCF's disclosure review program are expected to include artificial intelligence and registrants' potential exposure to changes in the commercial real estate market.

## SEC rulemaking updates

### **SEC amends Regulation S-P to enhance the protection of customer information**

The SEC **adopted** amendments to Regulation S-P to require broker-dealers, investment companies, registered investment advisers and transfer agents to adopt written policies and procedures to safeguard customer information and properly dispose of consumer report information. The amendments require these institutions to:

- ▶ Create an incident response program to detect, respond to and recover from unauthorized access to or use of customer information
- ▶ Provide timely notification to affected individuals whose sensitive customer information was, or is reasonably likely to have been, accessed or used without authorization

Larger entities, as defined in the amendments, will have until 3 December 2025 to comply with the amendments, and smaller entities will have until 3 June 2026.

### **SEC amends requirements for offerings of index-linked and variable annuities**

The SEC **amended** the rules on offerings of registered index-linked annuities and registered market value adjustment annuities to (1) require registration on Form N-4, (2) permit the use of the summary prospectus framework and (3) extend the applicability of Rule 156 of the Securities Act of 1933, which interprets when sales literature is materially misleading under federal securities laws, to non-variable annuity issuers.

The amendments are effective 60 days after publication in the Federal Register. Issuers will have until 1 May 2026 to comply with most of the amendments to Form N-4 and the related rule and form amendments. The compliance date for Rule 156 is the effective date.

### **Appeals court vacates SEC's private fund rules**

The US Court of Appeals for the Fifth Circuit vacated the SEC's **private fund adviser rules** adopted in August 2023 on the basis that the Commission exceeded its statutory authority under the Investment Advisers Act of 1940 in adopting the rules. The court's decision will stand, and the rules will be nullified before the first compliance date unless they are overturned on appeal by a higher court or the SEC seeks emergency relief to delay the decision. The SEC is assessing whether to appeal or take other action.

### **Appeals court partially vacates SEC's rescission of proxy voting advice rules**

The US Court of Appeals for the Fifth Circuit vacated the SEC's 2022 **rescission** of the notice-and-awareness requirements of the **proxy voting advice rules**, which were originally adopted in July 2020. The court said the SEC's explanation for the rescission was "arbitrary and capricious and therefore unlawful." The SEC has not commented yet on how it will respond to the decision.

### **SEC, FinCEN propose customer identification program requirements**

The SEC and the US Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) **proposed** new requirements for SEC-registered investment advisers and exempt reporting advisers to establish, document and maintain written customer identification programs that (1) verify the identity of each customer to the extent reasonable and practicable and (2) maintain records of the information used to verify a customer's identity.

The proposal is intended to prevent individuals from using false identities to establish customer relationships with investment advisers for the purposes of laundering money, financing terrorism or engaging in other illicit finance activity.

Comments are due by 22 July 2024.

## SEC staff guidance updates

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### EY resources

- ▶ [Technical Line, A closer look at the SEC's new rules on cybersecurity disclosures](#)

### SEC staff clarifies guidance on cybersecurity incident reporting

Mr. Gerding **clarified** that a company that chooses to voluntarily disclose a cybersecurity incident determined not to be material or for which a materiality determination has not yet been made should not make the disclosure under Item 1.05 of Form 8-K. Instead, companies are encouraged to disclose the incident under a different item of Form 8-K, such as Item 8.01.

Mr. Gerding said a company that discloses an immaterial incident (or one for which it has not yet made a materiality determination) under Item 8.01 and subsequently determines the incident is material should file under Item 1.05 on Form 8-K within four business days of that determination.

In response to concerns that the required Item 1.05 disclosures may preclude a company from sharing additional information with others, Mr. Gerding **clarified** that Item 1.05 does not prohibit the sharing of information beyond that included in Form 8-K. He reminded registrants that discussions regarding a cybersecurity incident could implicate the selective disclosures rules in Regulation FD, depending on the information disclosed and to whom that information is disclosed.

Mr. Gerding also suggested there are ways companies can privately share additional information about a material cybersecurity incident without implicating Regulation FD, and exclusions from Regulation FD may apply.

### SEC staff publishes guidance on cybersecurity incidents involving ransomware

The SEC staff **published** C&DIs relating to the disclosure of material cybersecurity incidents involving ransomware payments under Item 1.05 of Form 8-K to clarify the following:

- ▶ A ransomware payment made by a registrant and the subsequent cessation or apparent cessation of the related cybersecurity incident does not relieve the registrant of the requirement to determine the materiality of the incident and disclose the incident when required. The registrant cannot conclude that the incident is immaterial simply because of the incident's cessation.
- ▶ A registrant cannot necessarily conclude that a cybersecurity incident is immaterial based only on the size of the ransomware payment or on whether the registrant is reimbursed for the ransomware payment under an insurance policy.
- ▶ Disclosure of a series of ransomware attacks over time, either by a single threat actor or multiple threat actors, may be required even if the registrant determines that each incident is individually immaterial.

### SEC staff addresses the application of IFRS 19 in SEC filings

Mr. Gerding and SEC Chief Accountant Paul Munter **stated** that financial statements prepared under International Financial Reporting Standard (IFRS) 19, *Subsidiaries without Public Accountability: Disclosures*, that are included in SEC filings (e.g., in accordance with Rule 3-05 or Rule 3-09 of Regulation S-X) may not be sufficient to satisfy the needs of investors in the US public securities market. In such instances, the SEC staff believes that the requirements of IFRS 19 are likely to necessitate additional disclosures in financial statements filed with the SEC.

IFRS 19 allows eligible subsidiaries to provide reduced disclosures compared to those required under other IFRS accounting standards, while maintaining compliance with the recognition, measurement and presentation requirements under other IFRS accounting standards.

#### EY resources

- [Technical Line, \*Navigating the requirements for merging with a special purpose acquisition company\*](#)

### **SEC staff publishes compliance guide for small entities on new SPAC rules**

The SEC staff **published** a *Small Entity Compliance Guide* to address compliance with the Commission's new special purpose acquisition company (SPAC) rules, which were **adopted** in early 2024.

## **Personnel changes**

### **SEC reappoints Williams as PCAOB Chairperson**

The SEC appointed Erica Y. Williams to a second term as PCAOB Chairperson, beginning 25 October 2024 through 24 October 2029. Chair Williams began her current term on 10 January 2022.

## **Enforcement activities**

### **Global financial exchange charged with failing to notify the SEC of cyber intrusion**

The SEC charged a global financial exchange and its subsidiaries with failing to inform the SEC of a cyber intrusion in a timely manner as required by Regulation Systems Compliance and Integrity (Regulation SCI).

The SEC order alleged that the company did not comply with its internal cyber incident reporting procedures in a timely manner and, as a result, its subsidiaries did not immediately notify the SEC as required under Regulation SCI for events not immediately determined to be de minimis.

Without admitting or denying the SEC's findings, the company and its subsidiaries agreed to a cease-and-desist order and to pay a \$10 million civil penalty.

### **SEC charges services provider with cybersecurity-related internal control failures**

The SEC charged a global business communication and marketing services provider with failing to design effective disclosure controls and procedures to report relevant cybersecurity information to management with the responsibility for making disclosure decisions. As a result, the company allegedly failed to carefully assess and respond to a ransomware network intrusion in a timely manner.

The SEC order further alleged that the company failed to devise and maintain a system of cybersecurity-related internal accounting controls sufficient to provide reasonable assurances that access to the company's information technology systems and networks was permitted only with management's authorization.

Without admitting or denying the SEC's findings, the company agreed to a cease-and-desist order and to pay a \$2.1 million civil penalty.

### **SEC charges manufacturer with accounting, reporting and control failures**

The SEC charged an aerospace structural products manufacturer with financial reporting, accounting and internal controls violations that occurred over a six-year period and resulted in multiple restatements of its financial statements and material weaknesses in its internal control over financial reporting, including failure to retain personnel with approval knowledge of financial accounting and insufficiently documented accounting policies and procedures.

Without admitting or denying the SEC's findings, the company agreed to a cease-and-desist order and to undertakings to, among other things, fully remediate outstanding material weaknesses and have effective disclosure controls and procedures by stipulated dates. If the company fails to satisfy all of the undertakings, it will pay a \$400,000 civil penalty.

### What's next at the SEC?

The SEC's recently released **Spring 2024 regulatory agenda** reflects the priorities of Chair Gary Gensler, and indicates that much of the Commission's anticipated rulemaking activity, including proposed rules on corporate board diversity and the definition of securities held of record, has been pushed out to 2025, after the upcoming presidential election. Proposed rules on human capital management disclosures and incentive-based compensation arrangements at certain financial institutions are slated for the fall of 2024.

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