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**COVID-19 Disclosures:  
Not Just Speculation Anymore  
Attorney Laura Anthony Reports  
New Pubco Regulations**

**White Paper  
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## COVID-19 Disclosures: Not Just Speculation Anymore Attorney Laura Anthony Reports New Pubco Regulations

Now that the market can review and dissect two quarters of COVID-related disclosures and reporting companies are gearing up for third-quarter reporting, COVID disclosures are no longer pure speculation. Following the two official guidelines released by the SEC ([Disclosure Guidance Topic No. 9A](#) which supplemented the previously issued [Topic No. 9](#)), a new CD&I issued on COVID-19 executive employment benefits, and numerous unofficial statements and speeches on the topic, the investment community and reporting companies are navigating the areas that require the most attention and thoughtful disclosure. Not surprisingly, the areas requiring the greatest consideration are management, discussion and analysis (including human capital disclosures and forecasting), risk factors, and internal controls over financial reporting.

### COVID-19 “Benefits” – SEC Issues New C&DI

On September 21, 2020, the SEC issued a new compliance and disclosure interpretation (C&DI) related to the reporting of compensation perks or benefits. In particular, the SEC stated that:

In reporting compensation for periods affected by COVID-19, questions may arise as to whether benefits provided to executive officers because of the COVID-19 pandemic constitute perquisites or personal benefits for purposes of the disclosure required by Item 402(c)(2)(ix)(A) and determining which executive officers are “named executive officers” under Item 402(a)(3)(iii) and (iv). The two-step analysis articulated by the Commission in Release 33-8732A continues to apply when determining whether an item provided because of the COVID-19 pandemic constitutes a perquisite or personal benefit.

- An item is not a perquisite or personal benefit if it is integrally and directly related to the performance of the executive’s duties.
- Otherwise, an item that confers a direct or indirect benefit and that has a personal aspect, without regard to whether it may be provided for some business reason or for the convenience of the company, is a perquisite or personal benefit unless it is generally available on a non-discriminatory basis to all employees.

Whether an item is “integrally and directly related to the performance of the executive’s duties” depends on the particular facts. In some cases, an item considered a perquisite or personal benefit when provided in the past may not be considered as such when provided as a result of COVID-19. For example, enhanced technology needed to make the CEO’s home his or her primary workplace upon imposition of local stay-at-home orders would generally not be a perquisite or personal benefit because of the integral and direct relationship to the performance of the executive’s duties. On the other hand, items such as new health-related or personal transportation benefits provided to address new risks arising because of COVID-19, if they are not integrally and directly related to the performance of the executive’s duties, may be perquisites or personal benefits even if the company would not have provided the benefit but for the COVID-19 pandemic, unless they are generally available to all employees.

Although not tied into COVID, a week after issuing the new C&DI, the SEC filed settled enforcement charges against Hilton Worldwide Holdings for failing to fully disclose perquisites and personal benefits provided to executive officers. This is clearly a topic the SEC is paying attention to.



## Management's Discussion and Analysis of Financial Condition and Results of Operation (MD&A)

Item 303 of Regulation S-K (MD&A) requires discussions on liquidity, capital resources, results of operations, off-balance-sheet arrangements, and contractual obligations including any material changes. For example, Item 303 requires disclosure of "known trends or any known demands, commitments, events or uncertainties that will result in or that are reasonably likely to result in the registrant's liquidity increasing or decreasing in any material way." It also requires disclosure of unusual or infrequent events or transactions or any significant economic changes that materially affected the amount of reported income from continuing operations as well as known trends or uncertainties that have had or that the the company reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations.

In January 2020, the SEC issued interpretative guidance on MD&A (see [HERE](#)) reminding companies to include information not specifically referenced in the item that the company believes is necessary to an understanding of its financial condition, changes in financial condition and results of operations. COVID-19 has made MD&A a source of heartburn for most companies.

A part of MD&A necessarily involves a level of forecasting, especially related to liquidity and cash flows and uses (in addition to the obvious forecasting included in earnings releases and published guidance – see [HERE](#)). The COVID pandemic has affected different companies and sectors of the economy dramatically differently, with some struggling to get back to pre-outbreak operations (airlines) and others benefiting (Amazon). Either way, management has to use all of its available resources to provide meaningful MD&A disclosure on the results of operations for current periods and potential future impacts and changes. Moreover, it is likely that the world will not simply return to pre-COVID growth and operations, but rather, there could be a permanent shift in business models as a result of the pandemic.

Some steps management can take to assist in forecasting include (i) focusing on factors that the management can control and that are known; (ii) automating operational data to the greatest extent possible to maintain real-time updated information; and (iii) modeling different scenarios and weighing which ones seem most likely in light of current information.

In addition to operational changes, whether positive or negative, management has been carefully considering and disclosing the impact COVID has had on various expenses such as work-from-home changes or the restructuring of severance, impairments or stock incentive plans. Some expenses and write-downs have evolved into ordinary as opposed to unusual or non-recurring. On the flip side, a company must disclose the receipt of government assistance and the impact that is having on liquidity and the likely impact when such assistance is used up and no longer available.

Although there is an outstanding proposed rule amendment which would alter this structure, the substantive information that must be disclosed by management, including information related to COVID-19 and its impact on a business, would remain unchanged.

## Risk Factors

COVID-19 risk factors are now included in close to 100% of periodic reports that require risk factor disclosures and likewise in close to 100% of Securities Act and Exchange Act registration statements. As a reminder, smaller reporting companies are not required to include risk factors in their Exchange Act reports though they are required in all registration statements and Regulation A offering circulars.

Almost all companies, whether truly directly impacted or not, now include general risk factors related to uncertainty regarding the duration of the COVID-19 pandemic, the impact of the economic downturn, and changes in consumer





behaviors both during and after the pandemic. In addition, almost all companies in which such disclosures could be applicable, include general risk factors regarding travel and energy, work-from-home practices and governmental stay-at-home orders.

## Internal Controls over Financial Reporting (ICFR)

One of the most difficult aspects of managing the COVID-19 crisis has been the impact on internal controls over financial reporting (ICFR). In particular, managing remote workforces, the sometimes drastic impacts on income and expenses, government-mandated shutdowns, cluster breakouts in some businesses, and controlling the expenditures of government PPP loans have all had a direct impact on ICFR.

In addition to the high level necessity of ensuring that ICFR procedures make certain that transactions are executed in accordance with management's general or specific authorization and recorded as necessary to permit preparation of financial statements in conformity with US GAAP or International Financial Reporting Standards (IFRS), ICFR procedures include ensuring that access to assets, including cash and inventory, is only had in accordance with management's instructions or authorization. Recorded accountability for assets must be compared with the existing assets at reasonable intervals and appropriate action be taken with respect to any differences. COVID-19 necessarily has an impact on these responsibilities.

It is vitally important that a company carefully review its ICFR, including with the advice of professionals, and make adjustments to be sure that proper controls are and remain in place. Potential and actual disruptions to a company's supply chain, customer base, operations, processes and workforce should be weighed when evaluating the operating effectiveness of legacy controls. In situations in which the responsibilities for controls have been reassigned because of changes in personnel, companies should specifically evaluate whether appropriate segregation of duties continues to exist. Technology and cyber-security must also be reviewed to be sure that remote workers can continue to perform effectively.

Some companies are adapting quickly implementing video technology for inventory and asset review and improved technology, including blockchain, for real-time assessments.

It is also important that management's assessment over internal controls in the body of Forms 10-Q and 10-K be carefully reviewed to ensure that any deficiencies created by COVID-19 are disclosed together with remedial measures.

## Non-GAAP – EBITDAC Reporting

Since COVID began, some companies have created a new metric of for reporting financial results – earnings before interest, taxes, depreciation, amortization, and COVID – or EBITDAC. The form of EBITDAC varies with some companies adjusting EBITDA for COVID-19-related expenses or presenting gross margin without COVID-19 impacts.

Despite the natural inclination to want to disclose to the marketplace that, but for COVID, results of operations would be better than they actually are, the SEC is scrutinizing any such creative financial metric. Also, Topic 9 specified that the SEC does not think it is appropriate to present non-GAAP financial measures or metrics for the sole purpose of presenting a more favorable view of the company. Any metric must include an explanation as to why management finds the measure useful and how it helps investors assess the impact of COVID on the company's financial position and results of operations.

Also, it is important that companies remember that whenever presenting a figure or metric that is non-GAAP, it must comply with Regulation G or Item 10 of Regulation S-K, including providing a reconciliation to GAAP numbers, the reasons for presenting the non-GAAP numbers and particulars on the presentation and formatting of the information – see [HERE](#).



## The Author

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[Palm Beach securities attorney Laura Anthony](#) and her experienced legal team provide ongoing corporate counsel to small and mid-size private companies, OTC and exchange traded public companies as well as private companies going public on the Nasdaq, NYSE American or over-the-counter market, such as the OTCQB and OTCQX. For more than two decades [Anthony L.G., PLLC](#) has served clients providing fast, personalized, cutting-edge legal service. The firm's focus includes, but is not limited to Regulation D and Regulation S and PIPE Transactions, securities token offerings and initial coin offerings, [Regulation A/A+ offerings](#), as well as registration statements on Forms S-1, S-3, S-8 and merger registrations on Form S-4; compliance with the Securities Exchange Act of 1934, including registration on Form 10, reporting on Forms 10-Q, 10-K and 8-K, and 14C Information and 14A Proxy Statements; all forms of going public transactions; mergers and acquisitions including both reverse mergers and forward mergers; applications to and compliance with the corporate governance requirements of securities exchanges including [Nasdaq](#) and [NYSE American](#). Palm Beach attorney Laura Anthony is also the author of [SecuritiesLawBlog.com](#), the producer and host of [LawCast.com](#), Corporate Finance in Focus, and a contributor to The Huffington Post and Law360.

[Ms. Anthony](#) is involved throughout the community of Palm Beach. She is on the board of directors for the American Red Cross for Palm Beach and Martin Counties, and provides financial support to the Susan Komen Foundation, Opportunity, Inc., New Hope Charities, the Society of the Four Arts, the Norton Museum of Art, Palm Beach County Zoo Society, the Kravis Center for the Performing Arts and several other organizations. She is also a financial and hands-on supporter of Palm Beach Day Academy, one of Palm Beach's oldest and most respected educational institutions. She currently resides in Palm Beach with her husband and daughter.

Ms. Anthony is an honors graduate from Florida State University College of Law and has been practicing law since 1993.

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