

made, not misleading.³³ MD&A must specifically focus on known material events and uncertainties that would cause reported financial information not to be necessarily indicative of future operating performance or of future financial condition.³⁴ Companies must determine, based on their own particular facts and circumstances, whether disclosure of a particular matter is required in MD&A. However, the effectiveness of MD&A decreases with the accumulation of unnecessary detail or duplicative or uninformative disclosure that obscures material information.³⁵ Companies should view this guidance as an opportunity to evaluate whether there is information in their MD&A that is no longer material or useful, and therefore should be deleted, for example where there has been a change in their business or the information has become stale.

As the complexity of business structures and financial transactions increase, and as the activities undertaken by companies become more diverse, it is increasingly important for companies to focus their MD&A on material information. In preparing MD&A, companies should evaluate issues presented in previous periods and consider reducing or omitting discussion of those that may no longer be material or helpful, or revise

discussions where a revision would make the continuing relevance of an issue more apparent.

Companies also should focus on an analysis of the consolidated financial condition and operating performance, with segment data provided where material to an understanding of consolidated information. Segment discussion and analysis should be designed to avoid unnecessary duplication and immaterial detail that is not required and does not promote understanding of a company's overall financial condition and operating performance.

Both Instruction 4 to Item 303 of Regulation S-K and the 1989 Release address the requirement of discussion and analysis of changes in line items. A review of current MD&A provided by some companies, however, reveals that this is a portion of MD&A that can include an excessive amount of duplicative disclosure, as well as disclosure of immaterial items that do not promote understanding. The 1989 Release explicitly provides for the grouping of line items for purposes of discussion and analysis in a manner that avoids duplicative disclosure. In addition, Instruction 4 and the guidance in the 1989 Release do not require a discussion of every line item and its changes without regard to materiality. Discussion of a line item and its changes should be avoided where the information that would be disclosed is not material and would not promote understanding of MD&A.

Companies also must assess the materiality of items in preparing disclosure in their quarterly reports. There may be different quantitative and qualitative factors to consider when deciding whether to include certain information in a specific quarterly or annual report. The 1989 Release addresses some aspects of MD&A disclosure in the context of quarterly filings. That release clarifies that material changes to items disclosed in MD&A in annual reports should be discussed in the quarter in which they occur.³⁶ There also may be circumstances where an item may not be material in the context of a discussion of annual results of operations but is material in the context of interim results.

Disclosure in MD&A in quarterly reports is complementary to that made in the most recent annual report and in any intervening quarterly reports. Therefore, there may be cases, particularly where adequate disclosure is included in the MD&A in those earlier reports, where further disclosure in a

quarterly report is not necessary. If, however, disclosure in those earlier reports does not adequately foreshadow subsequent events, or if new information that impacts known trends and uncertainties becomes apparent in a quarterly period, additional disclosure should be considered and may be required.

3. Focus on Material Trends and Uncertainties

One of the most important elements necessary to an understanding of a company's performance, and the extent to which reported financial information is indicative of future results, is the discussion and analysis of known trends, demands, commitments, events and uncertainties. Disclosure decisions concerning trends, demands, commitments, events, and uncertainties generally should involve the:

- Consideration of financial, operational and other information known to the company;
- Identification, based on this information, of known trends and uncertainties; and
- Assessment of whether these trends and uncertainties will have, or are reasonably likely to have, a material impact on the company's liquidity, capital resources or results of operations.

As we have explained in prior guidance, disclosure of a trend, demand, commitment, event or uncertainty is required unless a company is able to conclude either that it is not reasonably likely that the trend, uncertainty or other event will occur or come to fruition, or that a material effect on the company's liquidity, capital resources or results of operations is not reasonably likely to occur.³⁷ (In this release we sometimes use the term "known material trends and uncertainties" to describe trends, demands, commitments, events or uncertainties as to which disclosure is required.)

In identifying known material trends and uncertainties, companies should consider the substantial amount of

³³ See Securities Act Rule 408 [17 CFR 230.408], Securities Exchange Act of 1934 Section 10(b) [15 U.S.C. 78j(b)], Exchange Act Rule 10b-5 [17 CFR 240.10b-5], and Exchange Act Rule 12b-20 [17 CFR 240.12b-20]. See also, *In the Matter of Edison Schools, Inc.*, Release No. 34-45925 (May 14, 2002) (finding, among other things, that the company failed to provide accurate and complete disclosure about its reported revenues); *In the Matter of Sony Corporation and Sumio Sano*, Release No. 34-40305 (Aug. 5, 1998) (finding that the company violated Section 13(a) of the Exchange Act by making inadequate disclosures about the nature and the extent of Sony Pictures' net losses and their impact on the consolidated results Sony was reporting); *In the Matter of Caterpillar Inc.*, Release No. 34-30532 (Mar. 31, 1992) (finding failure to disclose the impact of a subsidiary's foreign operations on the company's results of operations violated Section 13(a) of the Exchange Act).

³⁴ Instruction 3 to Item 303(a) of Regulation S-K [17 CFR 229.303(a)].

³⁵ See, e.g., Instruction 4 to Item 303(a) of Regulation S-K (indicating that repetition and line-by-line analysis is not required nor is it appropriate when the causes for a change in one line item also relate to other line items and indicating that, to the extent the changes from year to year are readily computable from the financial statements, the changes need not be recited in the discussion). The 1989 Release also addressed these points directly. See 1989 Release, Part III.D.

Where companies believe that information from the face of financial statements is helpful to readers in MD&A, they should consider using a tabular presentation that shows the decimal percentages of components or year-over-year percentage changes of the financial statement line items. An appropriate analysis of this data, to the extent that it is material, should accompany the tabular presentation consistent with the guidance in Section III.B.3 of this Release.

³⁶ See 1989 Release, Part III.E.

³⁷ See January 2002 Release at 3748 ("two assessments management must make where a trend, demand, commitment, event or uncertainty is known: 1. Is the known trend, demand, commitment, event or uncertainty likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required. 2. If management cannot make that determination, it must evaluate objectively the consequences of the known trend, demand, commitment, event or uncertainty, on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the registrant's financial condition or results of operations is not reasonably likely to occur" (citing the 1989 Release)).