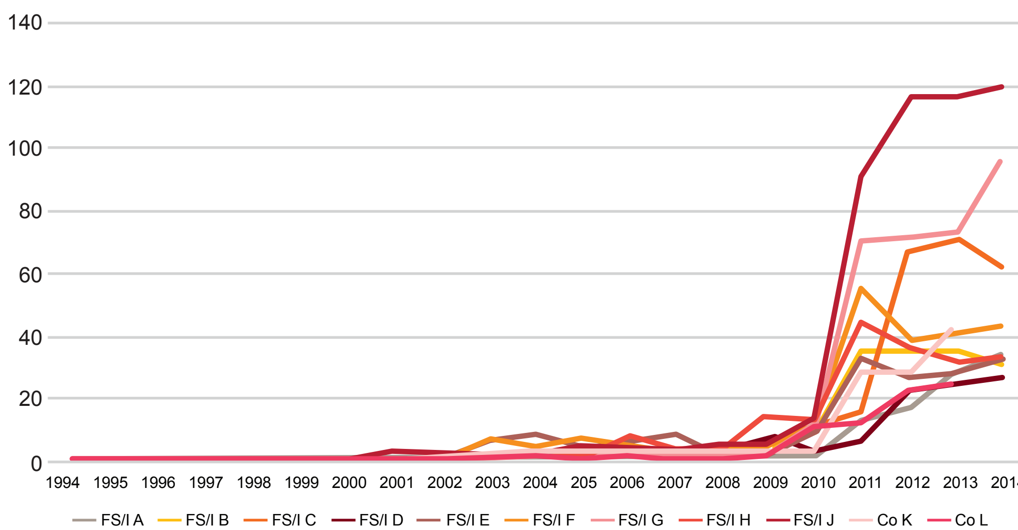
Disclosure reform: What do investors think?

June 2015

‘Disclosure reform’ is a topic frequently raised by SEC officials, securities lawyers, corporate secretaries, and academics. The topic can generate a lot of questions: Have currently mandated corporate reports gotten out of control, overwhelming investors and causing unnecessary costs to companies? Have our disclosure practices kept pace with developments in the types of information relevant to investors and the technological tools available to effectively analyze that information?

The primary goal of requiring publicly-traded companies to periodically disclose prescribed information is to feed the capital markets—and the investors who participate in them—with decision-relevant data that is comparable across companies. These requirements have been built over time, influenced by market events and changing attitudes. But two realities have impacted the evolutionary nature of corporate reporting. First, rarely is information removed from regulatory requirements, resulting in a steady increase (but not a corresponding decrease) in topics that must be addressed. Second, EDGAR, the SEC’s platform for corporate filings, does not include many of the technological tools that the public is accustomed to in other contexts—tools that ease access, search, and sorting of electronic data.

Growth of 10-K file size in megabytes



Source: George Washington University’s Institute for Corporate Responsibility and Center for Audit Quality, *Initiative on Rethinking Financial Disclosure* (Nov. 2014).

We expect a robust debate regarding what, when, and how companies in the future will report information to investors. To aid in that debate, we sought the views of those for whose benefit these requirements primarily exist: investors.

We reached out to the investment community to get their take on disclosure. We appreciate the input of those investors—20 diverse institutions representing almost $9 trillion in assets under management (AUM)—who agreed to be part of our pool. What did we want to know? We asked whether investors regularly read some portion of each of the documents that are part of the current disclosure system; what major topics within those documents are most helpful; how they usually access these documents; and in

“I believe we should rethink not only the type of information we ask companies to disclose, but also how that information is presented, where and how that information is disclosed, and how we can take advantage of technology to facilitate investors’ access to information and make it more meaningful to them.”

—SEC Chairman Mary Jo White, *The SEC in 2014* (41st Annual Securities Regulation Institute, Coronado, California), Jan. 27, 2014

what context they typically read them. We also asked our pool of investors to prioritize the relative importance of 10 key reporting areas, and we asked for their preliminary views on several ‘reforms’ that some commentators have already offered. So what did we find out? Five themes emerged:

1. **They do read.** The vast majority of investors report that they regularly read some portion of each of the SEC-mandated documents. Investors most frequently read the Management Discussion & Analysis (MD&A) portions of these documents, followed closely by the company’s analysis of risk factors and the audited financial statements.
2. **But not everything in detail.** While a significant number of investors report that they ‘regularly’ read every portion of each document included in our survey, some topics receive relatively less attention.
3. **Engagement is a key driver.** Investors are most likely to read these documents in the context of engaging with a company about its financial performance.
4. **Transparency around strategy is important.** Investors are generally very supportive of potential ‘reforms’ that would increase transparency around a company’s strategy (including more forward-looking information) and risk analysis. They are much more skeptical about suggestions that might reduce the information currently available to them.
5. **Support for short-form and new search tools.** Most investors believe that the technological/access ‘reforms’ that have been suggested by some commentators would help them. The strength of their views about the different options is somewhat variable, with strongest support expressed for a short-form/long-form concept, as well as enabling intuitive searches that do not require exact word matches. Support is more subdued for data visualization tools that enable comparison of selected line items in a historical context.

As the work of PwC’s Investor Resource Institute advances, we will continue to seek investor insights and share what we hear with the investment community, corporate officials, and regulators. Please watch our progress at www.pwc.com/us/en/pwc-investor-resource-institute.

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What do investors currently read—and why?

We asked investors about five documents that the Securities and Exchange Commission (SEC) requires publicly-traded companies to produce: annual report to shareholders, annual form 10-K, annual proxy statement, quarterly form 10-Q, and periodic form 8-K. We asked whether investors regularly read some portion of one or more of each of these documents and, for those who said no, we asked why. We also asked investors to identify the context in which they are most likely to read each document, as well as how they are most likely to access them.

A lengthy reading list

The vast majority of investors report that they regularly read some portion of each of these SEC-mandated documents.

What?	*Reasons why some investors say they don't regularly read*
Annual report to shareholders A state-of-the-company report, usually including a message from the Chief Executive Officer, audited financial statements, MD&A, new product plans, subsidiary activities, and results of operations	• Rely on a financial or proxy voting advisor for company-specific information
Annual Form 10-K An annual comprehensive overview of the company's business and financial condition (more incremental than the annual report to shareholders)	• Rely on a financial or proxy voting advisor for company-specific information • Get needed information from an analyst • Investment strategy does not require company-specific information
Annual Proxy Statement A description of the matters to be voted on at the company's annual meeting of shareholders, other corporate governance matters (e.g., descriptions of board committees, audit committee report, compensation committee report), and certain details about the company's executive compensation	• None offered
Quarterly Form 10-Q A periodic view of the company's financial position provided for each of the first three quarters of the company's fiscal year and includes unaudited financial statements; includes information about the quarter and year-to-date, as well as the comparable prior year period	• Get needed information from an analyst • Get needed information from financial press • Rely on a financial or proxy voting advisor for company-specific information • Investment strategy does not require company-specific information

Which topics are hot? Which are not?

Overall, investors most frequently read the MD&A portions of these documents, followed closely by the company's analysis of risk factors and the audited financial statements. Some topics—for example, information about a company's disclosure and financial reporting controls—are frequently of interest to about half of the investors in our pool. In contrast, other topics receive relatively less attention by most investors. These include mine safety disclosures and descriptions of new product plans. And when it comes to the annual proxy statement, most investors frequently read the compensation and audit committee reports, along with descriptions of the companies' governance policies and the compensation discussion and analysis (CD&A).

Investors' reading list

- MD&A
- Risk factors
- Audited financial statements

- Disclosure controls
- Financial controls

- Mine safety and new products

> ***"Condensing information is necessary because the current length of most reports is excessive and very difficult to manage. Focus on most relevant data."***
>
> —Portfolio manager, insurance company

> ***"Simplify disclosures. Avoid complex over-disclosure, but be specific about performance metrics and the rationale for strategic decisions. Use summaries. Use integrated reporting to communicate effectively in the form of a narrative that tells the company's story holistically."***
>
> —Director of corporate governance, family office

Information feeds engagement

Investors are most likely to read these documents in the context of engagement with the company about its financial performance. Investors engaging with a company to discuss various environmental, social, or governance (ESG) issues also frequently look to these documents for relevant information.

Investors are least likely to read these documents when considering whether to buy, sell, or hold a particular security.

40%

of investors respond that it is "very likely" they will engage with a company about its financial results.

60%+

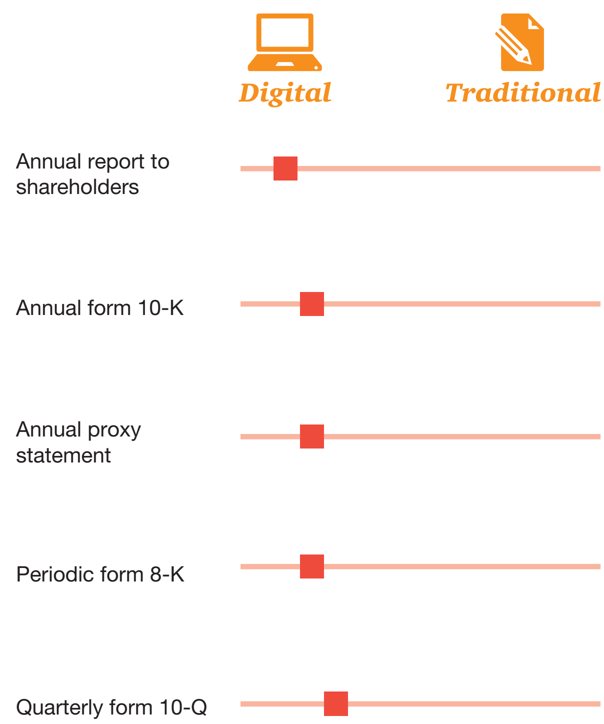
of investors consider it 'very likely' that they will engage with a company about various governance topics (including the company's overall governance profile, 'say on pay' vote results, and executive compensation).

Source: PwC, *2014 Investor Survey,* October 2014.

Electronic access is the key

Most of the investors we heard from are institutional (and not individual) investors, which may play a part in where they go to read these documents. The investors in our pool overwhelmingly look to electronic portals—either the company's website or the SEC's EDGAR database—rather than printed materials. These investors are just as likely to look to a company's website as they are to EDGAR.

How do investors read?



Note: *Digital* includes 'the SEC's website (EDGAR)' and 'the company's website.' *Traditional* includes 'printed materials sent from the company or a financial advisor' and 'other.'

What do investors want in the future?

Relative priorities

While some SEC-mandated corporate reporting requirements may be geared to the interests of other constituents, most serve primarily to provide investors with decision-relevant information. But what is relevant to different types of investors varies greatly, which likely contributes to the volume of current requirements. In an effort to gain insights into what information the broadest range of investors *most* value, we asked our investor pool to rank ten wide-ranging transparency topics, one through ten, according to their relative importance to corporate reporting. We weighted their responses,[1] which allowed us to see what topic was the highest priority for the most investors.

1. Current year financial statements
2. The company's analysis of the significant operational, market, and regulatory risks that it faces
3. The company's narrative explanation of its financial statements
4. Information about the compensation paid to the company's executives
5. Prior years' financial data in selected areas
6. Information about a company's disclosure controls and procedures and its internal controls over financial reporting
7. Information about significant legal proceedings
8. Information about the company's climate change preparedness and sustainability programs
9. Description of the company's main products and services
10. Information about the company's political activity and lobbying

"(I) would prefer an integrated report that summarized financial/sustainability risks and opportunities in a cohesive fashion, to allow an investor to see where the company is going and the risks and opportunities it will face, rather than just looking backward at prior performance, as most annual and sustainability reports do."

—ESG/Sustainability officer, asset manager

1 To determine the weighted rankings, we gave one point to every "1st priority" response, two points to every "2nd priority" and continuing to 10 points for every "10th priority." We then added up all points and ranked the topics from lowest points (indicating the highest priority) to highest points (indicating the relatively lowest priority).

Diving deeper into strategy, risk, and the future

Academics, securities lawyers, trade associations, and others have suggested potential changes to current disclosure rules, so we asked investors what they think about those changes. In general, we discovered that investors are supportive of potential changes that would increase transparency around a company's strategy, including more forward-looking information, and risk analysis.

"Increase the ease and cost of XBRL (eXtensible Business Reporting Language)."*

—Proxy voting officer, pension fund

"XBRL should be revived and should apply to proxy statements."

—-Director of corporate governance, asset manager

* XBRL is a freely available and global standard for exchanging business information, which simplifies and defines reporting terms.

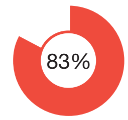
Reluctance to let go

Investors also indicated general skepticism about potential changes that might reduce the information currently available to them, perhaps an illustration of the difficulty posed by undertaking serious 'disclosure reform.'

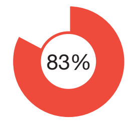
At first glance... what changes would investors back?

Generally support

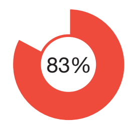
Include a requirement to discuss the company's strategy and forward-looking objectives



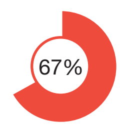
Disclose what the company does to mitigate identified risks



Include more analysis of risk factors (e.g., identifying those that are company-specific vs. non-company-specific and discussing both the impact on performance and likelihood of occurrence of each risk factor)



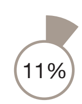
Adopt an 'integrated reporting' approach, through which a company's strategy, governance, and financial performance are presented in the context of the social, environmental, and economic context within which it operates



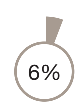
... and when would they balk?

Generally support

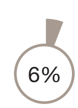
Replace all disclosure requirements that are currently triggered by specific quantitative thresholds with a general 'if material to the company' standard



Replace all detailed and specific disclosure requirements with general principles of reporting (this is also referred to as a 'principles-based' approach)



Eliminate Form 10-K (but keep the annual report to shareholders)



Technological innovations welcome

On the other hand, most investors say suggested technological changes would increase their use of these documents and improve the ease or effectiveness of their use.

Would technology change frequency or ease of use?

	Yes	*No*
Provide a short-form report (which would include a summary of period to period changes) that is separate from a long-form report (which would include more detailed discussion and areas that do not change period to period) and allow investors to choose which to read	100%	12%
Enable intuitive searches that do not depend on exact word matches	89%	22%
Provide data visualization tools that enable comparison of selected line items in a historical context	78%	33%
Present document topics in a selectable/collapsible format	88%	17%

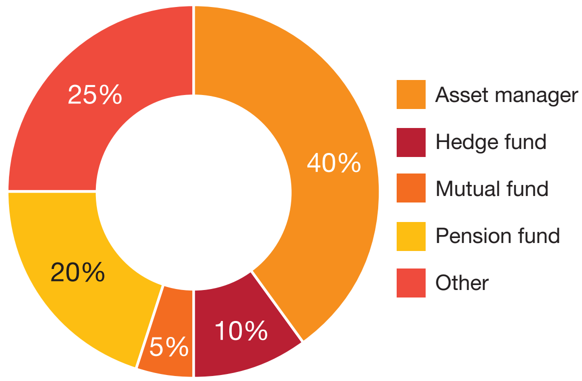
Note: Respondents were asked to select all that apply. *Yes* includes 'would probably increase the frequency of my use' and 'would probably make my current use easier or more effective.' *No* includes 'would probably not change how I use these materials' and 'I don't know.'

Information about investors in our pool

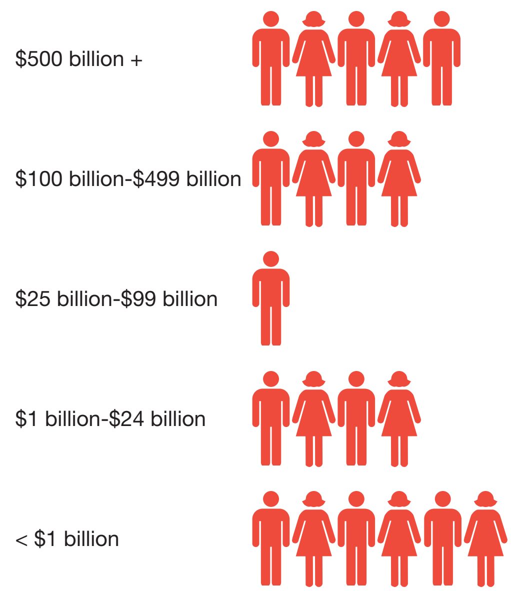
A diverse mix of institutional investors responded to our questions about disclosure. Forty percent are asset managers, and 20% are pension funds. The size of the investors in our pool was also diverse, with about the same number of very large (i.e., managing $500 billion or more) and very small (i.e., managing less than $1 billion) investors. In total, our pool consists of investors represent assets under management (AUM) of approximately $8.9 trillion.[2]

Most of our survey respondents have primary operations in the US and invest in markets across the globe. About a third of our respondents said their organization holds the stock of a US-listed company for an average of two to five years.

Demographics



Size of investors (by AUM)



2 To calculate AUM, we used the actual AUM as reported in each institution's public website. All of these values were retrieved on March 6, 2015, and if reported in other than US dollars were converted based on currency rates as of that same date. For the responses for which no AUM was public, we used $1,000. When the respondent declined to state its AUM, we used $0.

www.pwc.com/us/InvestorResourceInstitute

Additional information

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