

of OWB's mission in the upcoming fiscal year. We will continue to work to ensure that whistleblowers can freely report information to the Commission without fear of reprisal.

Proposed Amendments to Whistleblower Rules

Capitalizing on its nearly seven years of experience administering the whistleblower program, the Commission proposed amendments to the Whistleblower Rules during FY 2018 to build upon the success of the program. In addition to clarifying the requirements for anti-retaliation protection under the whistleblower statute, the proposed amendments would provide the Commission with additional discretion in making whistleblower awards to ensure that meritorious whistleblowers are appropriately rewarded for their efforts and increase efficiencies in the whistleblower claims review process. The proposing release was published in the Federal Register on July 20, 2018, and the comment period ended on September 18, 2018.²

Conclusion

The impact of the whistleblower program on the Commission's enforcement efforts and its contributions to the protection of Main Street investors continue to be strong. We are proud of the accomplishments of the whistleblower program in FY 2018. We look forward to the enduring success of the program in the years ahead.

ENDNOTES:

¹*Digital Realty Trust, Inc. v. Somers*, 138 S. Ct. 767, 200 L. Ed. 2d 15, 42 I.E.R. Cas. (BNA) 697, 102 Empl. Prac. Dec. (CCH) P 45981, Fed. Sec. L. Rep. (CCH) P 100021 (2018).

²Amendments to the Commission's Whistleblower Program Rules, 83 Fed. Reg. 34,702 (proposed July 20, 2018).

SEC/SRO UPDATE:

SEC IN SHUTDOWN; SEC PENALIZES ISSUER FOR PRESENTING NON-GAAP FINANCIAL MEASURES WITHOUT GIVING GAAP MEASURES EQUAL PROMINENCE; SEC ADOPTS RULE FOR DISCLOSURE OF HEDGING BY OFFICERS, DIRECTORS & OTHER EMPLOYEES

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SEC in Shutdown

At midnight on Friday, December 21, due to stalled negotiations between Congress and the President, the partial shutdown of the federal government shutdown began. Some agencies, such as the Department of Defense, already had funding in place, but many others did not, including independent agencies such as the Securities and Exchange Commission (SEC).

The SEC implemented its Operations Plan¹ for use during a lapse in appropriations when the partial shutdown began and determined that it had sufficient funds to continue operating until midnight on Wednesday, December 26. Accord-

ingly, the shutdown furlough began for SEC employees on Thursday, December 27. The SEC notified all employees of the furlough via email on that date.

SEC Staff

During the shutdown, SEC employees were divided into “excepted” and “non-excepted” employees.² Excepted employees are expected to continue working during the shutdown period and may telework with prior approval. With few exceptions relating to emergency situations, non-excepted employees *i)* may not serve as unpaid volunteers and must remain away from the work place; *ii)* should cease performing any work-related duties during the furlough; *iii)* should not provide information, answer questions, or offer to provide assistance to their office or their work colleagues during the furlough; and *iv)* should not telework or otherwise perform work from home or a remote location.

Each office and division is responsible for determining which positions are excepted, based in part on the job duties and position descriptions of each employee. Divisions and offices are responsible for continually reviewing the scope of duties necessary to support the protection of human life, the protection of property, or other excepted activities. The SEC has indicated that its needs may fluctuate throughout any lapse in appropriations and at times, more support may be needed, while at other times, minimal support will be needed. As a result, excepted status may change throughout any lapse in appropriations.

As of December 27, the SEC had put 94% of its staff on furlough, leaving at the agency a

skeleton crew of less than 300 employees to manage its essential operations.³

SEC Functions

The SEC indicated in its Operations Plan that while it is not possible to anticipate every SEC function that may be needed, the following is a summary of some of the major functions that the SEC will seek to continue during a lapse in appropriations:

- **EDGAR and Filer Support**—EDGAR is operated pursuant to a contract and will remain fully functional as long as funding for the contractor remains available through permitted means.
 - a) SEC personnel will be able to process requests for EDGAR access codes and password resets; answer questions about fee-bearing EDGAR filings and other emergency questions regarding EDGAR submissions.
 - b) However, the Divisions of Corporation Finance, Investment Management, and Trading and Markets, and the Office of Compliance Inspections and Examinations will be unable to process filings, provide interpretive advice, issue no-action letters, or conduct any other normal Division and Office activities.
 - c) As a result, new or pending registration statements or applications for exemptive relief will not be processed regardless of the status of any review of those filings.

- **IARD**—The Investment Adviser Registration Depository (IARD) system is operated pursuant to a contract and will remain fully functional and will continue to accept filings as long as funding for the contractor remains available through permitted means.
 - a) However, the Office of Compliance Inspections and Examinations will be unable to approve applications for registration by investment advisers; and the Division of Investment Management will be unable to provide interpretive advice regarding the Advisers Act, rules, or forms, or consider applications for exemptive relief under the Advisers Act.
 - b) As a result, new or pending investment adviser applications will not be processed.
 - c) The IARD system will continue to accept annual and other-than-annual amendments to Form ADV, Form ADV-W, and Form ADV-E filings.
 - **Tips, Complaints and Referrals**—The Division of Enforcement will have only a limited number of staff on duty to perform critical functions.
 - a) However, staff will attempt to respond to certain critical matters, including allegations of ongoing fraud and misconduct.
 - b) The Tips, Complaints, and Referrals website will continue to be operational and submissions will be reviewed for appropriate action.
 - **Investor Complaints**—The Office of Investor Education and Advocacy will have a limited number of staff on duty to review investor complaints submitted through the investor complaint form.
 - a) The Office will be unable to respond to complaints, questions, or requests for information.
 - **Comment Letters and Public Input**—The SEC will continue to accept comment letters during the federal government shutdown.
 - a) However, the Commission will have an extremely limited number of staff members on duty, so there will be delays in posting them to the SEC website.
- The following is a summary of some of the major SEC functions that will be discontinued during a lapse in appropriations:
- **Law Enforcement/Litigation**—Ongoing litigation, with certain exceptions; investigative work, including commencing investigations and conducting investigative testimony, except as necessary for the protection of property; pursuing the collection of any delinquent debts or work to distribute funds to harmed investors; and non-emergency examinations and inspections and related follow-up.
 - **Processing and Approvals of Filings and Registrations by Registrants and Regulated Entities**—Review and approval of applications for registration by entities (*e.g.*, investment advisers, broker-dealers,

transfer agents, nationally recognized statistical rating organizations, investment companies, and municipal advisors) and with respect to new financial products; review and approval of self-regulatory organization rule changes; review and acceleration of effectiveness of registration statements by issuers for securities offerings; review of periodic reports and other filings; and non-emergency support to registrants.

- **Rulemaking/Interpretive Questions/Exemptive Relief**—All non-emergency rulemaking; non-emergency interpretive advice, staff no-action letters, and processing new or pending applications for exemptive relief.
- **Oversight of Self-Regulatory Organizations and the Public Company Accounting Oversight Board**—Routine oversight of self-regulatory organizations and the PCAOB.
- **International Matters**—Non-emergency assistance to foreign authorities under bilateral or multilateral arrangements; and participation in multilateral organizations and working groups.
- **Other Discontinued Functions**—Processing of requests under the Freedom of Information Act absent a compelling need under 5 U.S.C.A. 552(a)(6)(E)(v)(I); all of the functions of the Equal Employment Opportunity Office; investor outreach and education, and monitoring investor toll-free telephone lines and emails from investors; routine human resources functions, including among others, training and de-

velopment; non-emergency travel; and routine public communications and operation of the Public Reference Room.

To assist registrants, the Division of Corporation Finance has posted several questions and answers on its website relating to operations generally and registration statements.⁴ The Division of Investment Management has stated that it will follow those procedures set forth by the Division of Corporation Finance, as applicable, with regard to the acceleration of initial registration statements and other types of filings made by registered investment companies during the federal government shutdown.⁵

Recent news articles have focused on the growing IPO backlog at the SEC as a consequence of the shutdown⁶ and the potential use and consequences of IPO filings employing rules that provide for automatic effectiveness without SEC review.⁷

On January 16, the SEC issued an order staying all pending administrative proceedings effective immediately, while providing parties to such proceeding an opportunity to seek removal of the stay under limited circumstances.⁸

The SEC's Operations Plan also contains policies and procedures for restarting agency functions when the lapse in appropriations ends.

SEC Penalizes Issuer for Presenting Non-GAAP Financial Measures Without Giving GAAP Measures Equal Prominence

On December 26, the SEC fined ADT Inc. over its failure to give Generally Accepted Accounting Principles (GAAP) equal prominence

to certain non-GAAP measures when presenting its financial numbers.⁹

SEC rules obligate companies to report under GAAP when presenting quarterly, annual, or current financial numbers. Companies may supplement those numbers with certain non-GAAP metrics, but they must give the GAAP numbers equal or greater prominence in their reporting.¹⁰ According to the enforcement action, ADT failed to do that in two of its earnings releases containing non-GAAP financial metrics—its Q4 2017 and Fiscal Year 2017 Earnings Release in March 2018 and its Q1 2018 Earnings Release in May 2018.

According to the SEC, in the headline of the Fiscal Year 2017 Earnings Release, ADT presented its adjusted EBITDA (a non-GAAP financial metric) for fiscal year 2017 and stated that the adjusted EBITDA was up 8% year-over-year, without also mentioning its GAAP net income or loss (the comparable GAAP financial measure) in the headline. The company also reported its earnings results similarly for the first quarter of 2018.

According to the SEC, in the Q1 2018 Earnings Release, ADT listed “FIRST QUARTER 2018 HIGHLIGHTS,” including bullet points noting (with dollar amounts) that adjusted EBITDA was up 7%, adjusted net income was up 26%, and adjusted net income per share was up 10%, but ADT failed to highlight GAAP financial measures in bullet points. According to the SEC, ADT had a net loss of \$157 million, greater than the year-earlier loss of \$141 million.

“When including a non-GAAP financial measure in a filing with the commission, (compa-

nies) must include a presentation, with equal or greater prominence, of the most directly comparable financial measure or measures calculated and presented in accordance with GAAP,” the SEC said in its enforcement announcement.

The SEC ordered ADT to cease and desist from committing or causing any violations and any future violations of the Securities Exchange Act of 1934 and ordered ADT to pay a civil money penalty of \$100,000 to the agency within 20 days of the entry of the order.

SEC Adopts Rule for Disclosure of Hedging by Officers, Directors & Other Employees

On December 18, the SEC issued a press release announcing the agency had approved final rules requiring companies to disclose their practices or policies with respect to hedging transactions by officers, other employees, and directors.¹¹ The final rules were published two days later and implement Section 14(j) of the Securities Exchange Act of 1934, which was enacted by Section 955 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.¹²

New Item 407(i) of Regulation S-K will require a company to disclose in proxy or information statements for the election of directors its practices or policies for officers, other employees, and directors relating to purchasing securities or other financial instruments, or otherwise engaging in transactions, that hedge or offset, or are designed to hedge or offset, any decrease in the market value of equity securities granted as compensation or held, directly or indirectly, by the officer, other employee, or director.

Companies may either summarize their prac-

tices or policies for these types of hedging activities or, alternatively, disclose their practices or policies in full. If a company does not have any such practice or policy, it must disclose that fact or state that hedging transactions are generally permitted.

The new item will require disclosure of practices or policies on hedging activities with respect to equity securities of the company, any parent or subsidiary of the company, or any subsidiary of any parent of the company.

Companies will be required to comply with the new disclosure requirements in proxy and information statements for the election of directors for fiscal years beginning on or after July 1, 2019. “Smaller reporting companies” and “emerging growth companies” will have an additional year to comply with the new disclosure requirements.

ENDNOTES:

¹See https://www.sec.gov/files/sec-plan-of-operations-during-lapse-in-appropriations-2018_0.pdf (Dec. 2018).

²In addition to the Operations Plan, the SEC posted an FAQ for its employees about the shutdown. See <https://www.sec.gov/files/sec-shutdown-furlough-faq.pdf> (as of Jan. 16, 2019).

³See Lara Crigger, “SEC Shutdown’s Impact of ETFs,” *ETF.com*, (Jan. 22, 2019), available at <https://www.etf.com/sections/features-and-news/sec-shutdowns-impact-etfs?nopaging=1>.

⁴See <https://www.sec.gov/page/corpfina-section-landing> (as of Jan. 22, 2019).

⁵See <https://www.sec.gov/investment-management> (as of Jan. 22, 2019).

⁶See Michelle Fox, “This was supposed to be a big year for IPOs, but the government

shutdown could ruin it,” *CNBC.com* (Jan. 9, 2019), available at <https://www.cnbc.com/2019/01/09/government-shutdown-could-ruin-big-year-for-ipos.html>.

⁷See Dave Michaels et al., “Companies Try to Skirt Shutdown’s IPO Limbo,” *Wall Street Journal* (Jan. 21, 2019), available at <https://www.wsj.com/articles/companies-try-to-skirt-shutdowns-ipo-limbo-11548066720>.

⁸See SEC Rel. No. 33-10602 (Jan. 16, 2019), available at <https://www.sec.gov/litigation/opinions/2019/33-10602.pdf>.

⁹See SEC Rel. No. 34-84956 (Dec. 26, 2018), available at <https://www.sec.gov/litigation/admin/2018/34-84956.pdf>.

¹⁰See Item 10(e)(1)(i)(A) of Regulation S-K.

¹¹See SEC Press Rel. No. 2018-291 (Dec. 18, 2018), available at <https://www.sec.gov/news/press-release/2018-291>.

¹²See SEC Rel. No. 33-10593 (Dec. 20, 2018), available at <https://www.sec.gov/rules/final/2018/33-10593.pdf>.