

PUBLICATION

SEC Amends Definition of 'Smaller Reporting Company'

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The Securities and Exchange Commission (SEC) has adopted amendments to its rules and forms to amend the definition of "smaller reporting company." Companies that qualify as smaller reporting companies can take advantage of scaled disclosure requirements in their SEC filings, including registration statements, annual reports on Form 10-K, and quarterly reports on Form 10-Q. Among other things, smaller reporting companies do not have to include a compensation discussion and analysis, pay ratio disclosure, and a number of compensation disclosure tables in their executive compensation discussions; are not required to provide a stock performance graph in their annual proxy statements; can omit the selected financial disclosure, supplementary financial information, and quantitative and qualitative disclosures about market risk otherwise required by various provisions of Regulation S-K; and are not required to include risk factor disclosure in their filings under the Securities Exchange Act of 1934 (Exchange Act) (though many do).

Currently, a company qualifies as a smaller reporting company if, as of the date such determination is made, its public float (the market value of its voting and non-voting common equity held by non-affiliates) is less than \$75 million or, if it had no public float, its annual revenues were less than \$50 million during its most recently completed fiscal year for which audited financial statements are available. Under the amended rules, a company will qualify as a smaller reporting company if either (i) its public float is less than \$250 million or (ii) its revenues as of its most recently completed fiscal year for which audited financial statements are available were less than \$100 million and it has no public float or a public float of less than \$700 million. In other words, in addition to the increase in the determination thresholds, a company no longer has to have a zero public float in order to qualify as a smaller reporting company under the revenue test.

The amendments will be effective 60 days after the date that the adopting release is published in the *Federal Register*. The amendments do not change the date at which, or as of which these determinations must be made or the manner in which they are calculated; as a result, Exchange Act reporting companies will continue to calculate their public float annually, as of the first day of their fiscal year, based on the market value of their voting and non-voting common equity held by non-affiliates as of the end of the second quarter of the prior year. The adopting release clarifies that a company that did not qualify as a smaller reporting company under the current definition will so qualify if it meets one of the qualification standards in the amended rules when making the calculation for its first fiscal year ending after effectiveness of the amendments. For example, a calendar year-end company that had a public float greater than \$75 million as of June 30, 2017, and did not qualify for smaller reporting company status, but that had a public float of \$215 million as of June 29, 2018, will qualify as a smaller reporting company for the fiscal year ending December 31, 2019 (although as under current rules it can start complying with the scaled disclosure requirement beginning with its third quarter 2018 Form 10-Q), even though the amendments were not effective on June 29, 2018.

A company that does not qualify as a smaller reporting company when making its first calculation under the new standards may so qualify at a later date if it meets one or more of the lower qualification thresholds set forth in the amended rules, which are set at 80 percent of the initial qualification thresholds. So, a company that did not qualify as a smaller reporting company because its public float was not less than \$250 million will later qualify if its public float falls below \$200 million at a later measurement date. Under the revenue test, however, a company need only meet the lower threshold for the criteria it did not satisfy initially, and continue

to meet the threshold it did satisfy, in order to qualify as a smaller reporting company. Therefore, a company that at its initial measurement date had a public float of less than \$700 million but revenues of \$100 million or more will qualify as a smaller reporting company if at a later measurement date its revenues fall to less than \$80 million and it continues to have a public float of less than \$700 million. Conversely, a company that had revenues of less than \$100 million but a public float of \$700 million or more at its initial measurement date can qualify as a smaller reporting company at a later measurement date if its public float falls below \$560 million and its revenues remain at less than \$100 million – such company need not see its revenue fall to below \$80 million in order to qualify since it satisfied the revenue threshold at the initial measurement date.

Importantly, the SEC did not amend the definitions of "accelerated filer" and "large accelerated filer" other than to remove the exclusion from these definitions of any company that qualifies as a smaller reporting company. Therefore, companies with a public float of \$75 million or more (but less than \$700 million) will continue to be an accelerated filer even if they qualify as smaller reporting companies, and will have to comply with the reporting and other requirements applicable to accelerated filers; importantly, such companies will be required to obtain an auditor attestation of their internal control over financial reporting and comply with the accelerated timelines for Form 10-K (75 days after fiscal year end) and Form 10-Q (40 days after quarter end) filings applicable to accelerated filers. The adopting release and related press release note, however, that Chairman Clayton has directed the SEC Staff to "formulate recommendations to the Commission for possible additional changes to the "accelerated filer" definition that, if adopted, would have the effect of reducing the number of registrants that qualify as accelerated filers," so this may change in the future.

The SEC also amended Rule 3-05(b)(2)(iv) of Regulation S-X, which governs requirements for financial statements of businesses acquired or to be acquired. Currently, the rule allows certain registrants to omit such financial statements for the earliest of the three years required if the net revenues of the acquired (or to be acquired) business is less than \$50 million. As the \$50 million revenue figure is based on the revenue threshold in the smaller reporting company definition, the SEC has amended the rule to increase the revenue figure to less than \$100 million, consistent with the amendments to the smaller reporting company definition.