

Insights: Alerts

SEC Amends Definition of "Smaller Reporting Company"

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On June 28, the Securities and Exchange Commission (SEC) adopted amendments to the definition of "smaller reporting company" (SRC) to increase the number of companies eligible to comply with certain scaled disclosure requirements under the federal securities laws. The amendments will reduce compliance costs for companies covered under the broader SRC definition that elect to provide the scaled disclosure permitted to SRCs.

In addition, the amendments change the definitions of "accelerated filer" and "large accelerated filer" so that newly SRC-eligible companies continue to be subject to accelerating filing requirements. Moving forward, companies contemplating SRC status should take care in determining how the new rules pertaining to SRCs would interact and potentially affect their disclosure requirements.

Changes to the "Smaller Reporting Company" Definition

Under the new definition, a company that is not an investment company, an asset backed issuer, or a majority-owned subsidiary of a non-SRC company may become a SRC if (1) it has a public float of less than \$250 million as of the last business day of its most recently completed second fiscal quarter, or (2) it has no public float or a public float of less than \$700 million, and less than \$100 million of annual revenue during the most recently completed fiscal year for which audited financials are available.

The following chart compares prior and current threshold requirements under the SRC definition:

	Previous Definition of SRC	Amended Definition of SRC
(i) Public Float	Public float of less than \$75 million	Public float of less than \$250 million
(ii) Annual Revenue	Less than \$50 million in annual revenues and no public float	Less than \$100 million in annual revenues and:- no public float, or-public float of less than \$700 million

SRC scaled disclosure can apply, depending on the circumstances, to a company's annual and quarterly reports, proxy statements, and registration statements. In certain cases, scaled disclosure would permit, among other things, providing two (rather than three) years of audited financial statements, allowance to discuss two (rather than three) fiscal years in the Management's Discussion and Analysis of Financial Condition and Results of Operations, and significantly reduced narrative and tabular disclosure for executive compensation. Furthermore, SRC scaled

disclosure may be used in whole or in part at the SRC's election. A SRC can therefore choose to comply with the scaled disclosure in one or more instances that it is permitted or, alternatively, choose to comply with the broader disclosure requirements that apply to registrants that do not qualify for SRC status.

Under the new rules, a company that fails to qualify as a SRC on its annual determination date can obtain SRC status if the company meets a subsequent threshold or thresholds set at 80 percent of the initial threshold or thresholds that the company missed. Namely, a company must meet the following subsequent thresholds to obtain SRC status: (1) under the public float test: less than \$200 million in public float if the company exceeded \$250 million in public float previously and (2) under the revenue test: less than \$80 million in annual revenue if the company exceeded \$100 million in revenue previously and less than \$560 million in public float if it exceeded \$700 million in public float previously.

For the first fiscal year ending after the rules are effective, a company would qualify for SRC status if it meets one of the initial qualification thresholds in the amended definition as of the date it is required to measure its public float or revenues, even if the company would not have been eligible for SRC status under the pre-amendment definition.

Changes to "Accelerated Filer" Definition

Prior to the new rules, the definitions of "accelerated filer" and "large accelerated filer" in Exchange Act Rule 12b-2 excluded companies that would qualify as SRCs from their definitions. In order to preserve the public float requirements for accelerated filers and large accelerated filers in light of the increased breadth of the SRC definition, the SEC eliminated the exclusions for SRCs from the terms "accelerated filer" and "large accelerated filer." These changes retain the public float threshold for accelerated filers (of \$75 million or more, but less than \$700 million) and the corresponding threshold for large accelerated filers (of \$700 million or more).

As a result of these revisions, SRCs are no longer automatically considered non-accelerated filers. While the SEC staff has been directed to consider how the "accelerated filer" definition may be changed to limit the number of companies that are accelerated filers, newly eligible SRCs that meet the accelerated filer definition will continue to be subject to the accelerated filing requirements and the Sarbanes-Oxley Act auditor attestation requirements applicable to accelerated filers. Given the potential for future changes in this regulatory space, companies should remain apprised of further SEC action with respect to the "accelerated filer" definition.

Changes to Financial Statements of Certain Acquired Businesses

Lastly, Rule 3-05 of Regulation S-X requires the inclusion of financial statements of businesses acquired or to be acquired in certain registration statements and current reports. Previously, Rule 3-05 allowed certain registrants to omit financial statements for the earliest of the three fiscal years required by Rule 3-05 if the net revenues of the acquired business were less than \$50 million in its most recent fiscal year. Recognizing that the \$50 million threshold was tied to the revenue threshold in the SRC definition, the SEC revised Rule 3-05 to increase the revenue threshold for omitting certain financial statements for acquired or to be acquired businesses to \$100 million.

The final rules will become effective September 10, 2018.

Footnotes

¹ For example, a registrant with a September 30 fiscal year end that previously would not qualify as a SRC and that had a public float of \$220 million as of March 30, 2018 (the last business day of the registrant's most recently completed second quarter) would qualify as a SRC for the fiscal year ending September 30, 2018. *Securities and Exchange Commission, Release Nos. 33-10513; 34-83550; File No. S7-12-16.*

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