



## Rule changes mean more public companies qualify for “smaller reporting company” relief

By David R. Brown and Erensu Altan

Effective as of Monday, September 10, under final rules recently issued by the SEC, more reporting companies will be eligible for “smaller reporting company” (SRC) status. SRCs are eligible for reduced disclosure obligations—called “scaled disclosure accommodations”—for registration statements, periodic reports and proxy statements. The reduced disclosures include, among other things, (a) financial statements, management discussion and analysis (MD&A) and executive compensation information covering two years instead of three years, (b) no compensation discussion and analysis (CD&A) and (c) omission of risk factors in certain filings. These optional scaled requirements can be selected on an item-by-item basis. The SEC estimates that nearly 1,000 more companies will qualify as SRCs over the next year.

### New SRC initial qualification thresholds

A reporting company may qualify as an SRC under either of two tests. The first, the “public float test,” measures the issuer’s public float (that is, the market value of outstanding shares held by non-affiliates). Under the prior rules, a public float of less than \$75 million qualified a reporting company for SRC status. The new rules increase this threshold to \$250 million. The second, the “revenue test,” measures the issuer’s revenues alongside its public float. Under the prior rules, annual revenues of less than \$50 million, combined with no public float, qualified an issuer for SRC status. As revised, annual revenues of less than \$100 million, combined with a public float of less than \$700 million, are required.

### Revised SRC subsequent qualification thresholds

The new rules will also affect “subsequent qualification thresholds,” that is, the SRC qualification thresholds for an issuer that did not qualify as an SRC for the previous year under the public float or revenue test. These have been reset at 80% of the new initial SRC qualification thresholds summarized above (i.e., \$200 million public float under the public float test and \$80 million in revenue and \$560 million public float under the revenue test.)

### Impact on accelerated filer status

The changes to the SRC rules have an impact on “accelerated filer” status as well. Accelerated filers have shortened filing deadlines for periodic reports and must provide an auditor’s attestation as to

management's assessment of internal controls, as required by Section 404(b) of the Sarbanes-Oxley Act. Previously, SRCs by definition could not be "accelerated filers" because a public float of at least \$75 million was required for accelerated filer status. However, the new SRC thresholds summarized above do not alter the existing accelerated filer thresholds, so a newly eligible SRC with a public float of \$75 million or more will remain an accelerated filer, albeit with the possibility of scaled disclosure accommodations. Jay Clayton, the chairman of the SEC, has directed the SEC's staff to recommend potential changes to the definition of accelerated filer that would reduce the number of registrants that so qualify. It seems likely that future rule changes could align the accelerated filer thresholds with the revised SRC thresholds.

## **Changes to financial statement requirements for certain acquisitions**

The SEC also adopted changes to the requirements under Rule 3-05(b)(2)(iv) of Regulation S-X regarding the net revenue threshold for acquired businesses. Previously, a reporting company that acquired a business with revenues in excess of \$50 million was required to include in registration statements and current reports on Form 8-K financial statements for the acquired business for the last three fiscal years. The revised rule increases this threshold to \$100 million.

## **Looking ahead**

The new rules are effective September 10, 2018, and will apply to an issuer's first fiscal year ending after that date. For newly eligible SRCs, they may bring welcome relief in the form of scaled disclosure accommodations, although we expect that many issuers will opt to continue making the more complete disclosures previously required of them, owing to investor expectations. For reporting companies making acquisitions between \$50 million and \$100 million, the revised reporting requirements have the potential to reduce the cost of integrating, and reporting on, acquired businesses with revenues between the old and new thresholds. We expect that these changes are only the first of several additional measures to follow from the SEC designed to provide further scaled disclosure requirements for smaller public companies.

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