

CLIENT ALERT

# SEC Proposes to Exempt Additional Companies from Auditor Attestation Requirement

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The Securities and Exchange Commission recently proposed amendments<sup>1</sup> to the definitions of accelerated filer and large accelerated filer to exempt certain smaller reporting companies (“SRCs”) from the requirement, under Section 404(b) of the Sarbanes-Oxley Act, to have their independent auditors attest to management’s assessment of the effectiveness of their internal control over financial reporting. Like other recent SEC proposals,<sup>2</sup> the proposed amendments aim to promote capital formation by reducing compliance costs, particularly for smaller reporting issuers, following the expansion of the definition of SRC last year, which created overlaps with the accelerated filer and large accelerated filer definitions.<sup>3</sup>

Under the current definitions, because the public float test in the SRC and accelerated filer definitions overlap, an issuer meeting the accelerated filer definition<sup>4</sup> will be both an SRC and an accelerated filer if it has: a) a public float, measured as of the last business day of its most recently completed second fiscal quarter, of \$75 million or more, but less than \$250 million, regardless of its annual revenues; or b) less than \$100 million in annual revenues, and a public float of \$250 million or more, but less than \$700 million. As a result, these SRCs would be required, in addition to having their

<sup>1</sup> See SEC Release No. 34-85814, *Amendments to the Accelerated Filer and Large Accelerated Filer Definitions*, May 3, 2019, available [here](#).

<sup>2</sup> See, for example, our recent client alert *SEC Proposes Simplifying Financial Disclosures Relating to Acquisitions and Dispositions*, May 13, 2019, available [here](#).

<sup>3</sup> The SRC definition was expanded to enable more companies to qualify for the scaled disclosure accommodations applicable to SRCs. See our client alert *SEC Expands “Smaller Reporting Company” Definition*, July 9, 2018, available [here](#).

<sup>4</sup> Under Securities Exchange Act Rule 12b-2, to be an accelerated filer, an issuer also must have been subject to the requirements of Exchange Act Section 13(a) or 15(d) for a period of at least twelve calendar months and have filed at least one annual report pursuant to those sections.

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management assess the effectiveness of their internal control over financial reporting, to have their independent auditors attest to such management's assessment.

To better balance the benefits and burdens of compliance mandates for these companies, the proposed amendments would exclude from the definitions of accelerated filer and large accelerated filer an issuer that has a public float of less than \$700 million but revenues of less than \$100 million, as summarized in the following table:

<u>Status</u>	<u>Current Rules</u>		<u>Proposed Rules</u>	
	<u>Public Float</u>	<u>Annual Revenues</u>	<u>Public Float</u>	<u>Annual Revenues</u>
SRC and Non-Accelerated Filer	Less than \$75 million	N/A	Less than \$75 million	N/A
			\$75 million to less than \$700 million	Less than \$100 million
SRC and Accelerated Filer	\$75 million to less than \$250 million	N/A	\$75 million to less than \$250 million	\$100 million or more
	\$250 million to less than \$700 million	Less than \$100 million		
Accelerated Filer (not SRC)	\$250 million to less than \$700 million	\$100 million or more	\$250 million to less than \$700 million	\$100 million or more

To avoid frequent changes of status, under current rules, once an issuer is an accelerated or large accelerated filer, it will not become a non-accelerated or accelerated filer until its public float falls below a specified threshold lower than the threshold that it had initially needed to become an accelerated or large accelerated filer. The proposed amendments modify these transition rules to set the exit thresholds for the public float test at 80% of their initial amounts, as described in the below table.

<u>Initial Public Float Determination</u>	<u>Resulting Filer Status</u>	<u>Current Rules</u>		<u>Proposed Rules</u>	
		<u>Subsequent Public Float Determination</u>	<u>Resulting Filer Status</u>	<u>Subsequent Public Float Determination</u>	<u>Resulting Filer Status</u>
\$700 million or more	Large Accelerated Filer	\$500 million or more	Large Accelerated Filer	\$560 million or more	Large Accelerated Filer
		Less than \$500 million but \$50 million or more	Accelerated Filer	Less than \$560 million but \$60 million or more	Accelerated Filer
		Less than \$50 million	Non-Accelerated Filer	Less than \$60 million	Non-Accelerated Filer
Less than \$700 million but \$75 million or more	Accelerated Filer	Less than \$700 million but \$50 million or more	Accelerated Filer	Less than \$700 million but \$60 million or more	Accelerated Filer
		Less than \$50 million	Non-Accelerated Filer	Less than \$60 million	Non-Accelerated Filer

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Consistent with the addition of the revenue test to the proposed amended SRC definition, the amendments would also add a revenue test to these transition rules for accelerated and large accelerated filers.

In making the proposal, the SEC noted that the newly exempted SRCs would remain subject to various other requirements, including the need for audited financial statements, which embody certain tests by the auditors of the issuer's internal controls, and the management effectiveness assessment itself. SEC Commissioner Robert J. Jackson, Jr., however, dissented from the proposal, stating that the amendments are based on outdated evidence and understate the benefits of the auditor attestation while exaggerating the benefits of its elimination for these smaller companies.<sup>5</sup>

The SEC is soliciting comments on the proposed amendments for a 60-day period following publication in the *Federal Register*.

If you have any questions regarding this client alert, please contact the following attorney or the Willkie attorney with whom you regularly work.

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<sup>5</sup> See *Statement on Proposed Amendments to Sarbanes Oxley 404(b) Accelerated Filer Definition*, May 9, 2019, available [here](#).