

CLIENT ALERT

SEC Expands “Smaller Reporting Company” Definition

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On June 28, 2018, the Securities and Exchange Commission adopted final rules amending the definition of “smaller reporting company” (SRC) to expand the number of companies that can benefit from certain scaled disclosure accommodations available to SRCs.¹ The change is designed to reduce compliance costs for registrants that qualify for SRC status under the expanded definition, thereby encouraging capital formation, while maintaining appropriate investor protections. The SEC estimates that close to a thousand additional companies will be eligible for SRC status under the new definition.

Background

The SEC established the SRC category in late 2007 to allow such companies to comply with certain scaled disclosure requirements, rather than those applicable to larger companies, in their SEC filings. For example, SRCs do not have to disclose as many years of audited financial statements and management’s discussion and analysis as non-SRCs. For a summary of the scaled disclosure accommodations available to SRCs (which are not being modified as part of these amendments), see [Appendix I](#) at the end of this memorandum.

Prior to the amendments, a company qualified as an SRC if:

- its public float was less than \$75 million, or
- it had no public float or market price for its equity and had less than \$50 million in annual revenues.

¹ See SEC Release No. 33-10513, *Amendments to Smaller Reporting Company Definition* (June 28, 2018), available [here](#).

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Qualifying as an SRC Under the Amendments

The amendments permit a registrant to qualify as an SRC based on a public float test or a revenue test. Under the final rules, which become effective 60 days following publication in the Federal Register, registrants qualify as SRCs if they have either

- a public float of less than \$250 million, or
- annual revenues of less than \$100 million and either no public float or a public float of less than \$700 million.

The following table summarizes the amendments to the SRC definition for a registrant making an initial determination under the amendments or a current SRC seeking to continue to qualify:

Initial SRC Determination		
Criteria	Prior Definition	New Definition
<i>Public Float</i>	Public float of less than \$75 million	Public float of less than \$250 million
<i>Revenues</i>	Less than \$50 million of annual revenues and no public float	Less than \$100 million of annual revenues and either: <ul style="list-style-type: none">• no public float, or• a public float of less than \$700 million

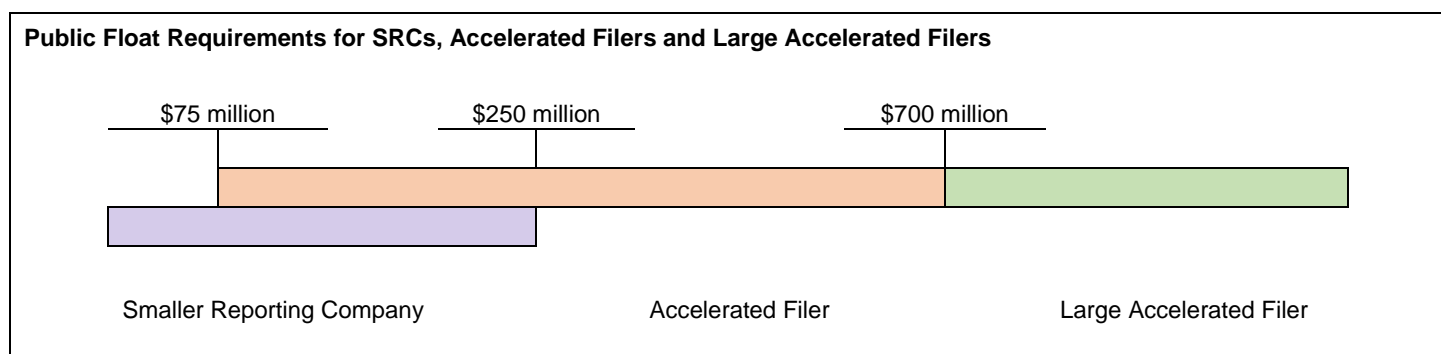
SRC status is determined on an annual basis, with the public float calculated as of the last business day of the company’s previous second fiscal quarter.

To avoid situations in which registrants frequently enter and exit SRC status due to small fluctuations in their public float, the rules provide thresholds for regaining SRC status in subsequent annual determinations if a registrant fails to meet the initial thresholds above. Once a registrant determines that it does not qualify as an SRC under the initial thresholds, it cannot subsequently qualify until its public float falls below a lower threshold, set at 80% of the initial qualification threshold. The amendments, consistent with the 80% ratio from the previous definition, establish lower qualification thresholds for subsequent annual determinations in light of the changes to the initial thresholds. The following table summarizes the changes:

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SRC Requalification		
Criteria	Prior Definition	New Definition
<i>Public Float</i>	Public float of less than \$50 million	Public float of less than \$200 million, if it previously had \$250 million or more of public float
<i>Revenues</i>	Less than \$40 million of annual revenues and no public float	<ul style="list-style-type: none"> • Less than \$80 million of annual revenues, if it previously had \$100 million or more; <i>and</i> • a public float of less than \$560 million, if it previously had \$700 million or more of public float

The definitions of “accelerated filer” and “large accelerated filer” were amended to preserve the existing public float thresholds and eliminate the automatic exclusion of SRCs from those definitions. Accelerated filers must comply with shorter filing deadlines for their annual and quarterly reports as well as the auditor internal control attestation requirements of Section 404(b) of the Sarbanes-Oxley Act. Under the new rules, some registrants will qualify as both SRCs and accelerated filers and, as a result, will need to comply with shorter filing deadlines and obtain an auditor attestation. The table below illustrates the overlap:



Recognizing this overlap, Chairman Clayton has directed the SEC staff to formulate recommendations for possible changes to reduce the number of registrants defined as accelerated filers, taking into account, among other things, the historical and current relationship between the SRC and accelerated filer definitions.

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

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Appendix I

Scaled Disclosure Accommodations for SRCs

Regulation S-K	
Item	Scaled Disclosure Accommodation
101 - Description of Business	<p>May satisfy disclosure obligations by describing the development of the registrant's business during the last three years rather than five years.</p> <p>Business development description requirements are less detailed than disclosure requirements for non-SRCs.</p>
201 - Market Price of and Dividends on the Registrant's Common Equity and Related Stockholder Matters	Stock performance graph not required.
301 - Selected Financial Data	Not required.
302 - Supplementary Financial Information	Not required.
303 - Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A")	<p>Two-year MD&A comparison rather than three-year comparison.</p> <p>Two-year discussion of impact of inflation and changes in prices rather than three years.</p> <p>Tabular disclosure of contractual obligations not required.</p>
305 - Quantitative and Qualitative Disclosures About Market Risk	Not required.
402 - Executive Compensation	<p>Three named executive officers rather than five.</p> <p>Two years of summary compensation table information rather than three.</p> <p>Not required:</p> <ul style="list-style-type: none"> • Compensation discussion and analysis ("CD&A"). • Grants of plan-based awards table. • Option exercises and stock vested table. • Pension benefits table. • Nonqualified deferred compensation table. • Disclosure of compensation policies and practices related to risk management. • CEO pay ratio disclosure.

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404 - Transactions With Related Persons, Promoters and Certain Control Persons ²	Description of policies/procedures for the review, approval or ratification of related party transactions not required.
407 - Corporate Governance	Audit committee financial expert disclosure not required in first annual report. Compensation committee interlocks and insider participation disclosure not required. Compensation committee report not required.
503 - Prospectus Summary, Risk Factors and Ratio of Earnings to Fixed Charges	No ratio of earnings to fixed charges disclosure required. No risk factors required in Exchange Act filings.
601 - Exhibits	Statements regarding computation of ratios not required.

Regulation S-X	
Rule	Scaled Disclosure Accommodation
8-02 - Annual Financial Statements	Two years of income statements rather than three years. Two years of cash flow statements rather than three years. Two years of changes in stockholders' equity statements rather than three years.
8-03 - Interim Financial Statements	Permits certain historical financial data in lieu of separate historical financial statements of equity investees.
8-04 - Financial Statements of Businesses Acquired or to Be Acquired	Maximum of two years of acquiree financial statements rather than three years.
8-05 - Pro Forma Financial Information	Fewer circumstances under which pro forma financial statements are required.
8-06 - Real Estate Operations Acquired or to Be Acquired	Maximum of two years of financial statements for acquisition of properties from related parties rather than three years.
8-08 - Age of Financial Statements	Less stringent age of financial statements requirements.

² Note that rather than a flat \$120,000 threshold for related party transaction disclosures, the threshold for SRCs is the *lesser* of \$120,000 and 1% of total assets, the only instance where the rules applicable to SRCs are more stringent than those for non-SRCs.