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To the Point

SEC – proposed rule

SEC proposes excluding some smaller reporting companies from accelerated filer status

The proposal would expand the exemption from the requirement to obtain an auditor's report on internal control to all smaller reporting companies with less than $100 million in revenue.

What you need to know

- The SEC proposed amending its rules to make all issuers that qualify as smaller reporting companies and have less than $100 million in annual revenue non-accelerated filers.
- Issuers that would become non-accelerated filers would have extended filing deadlines and would no longer be required to obtain an annual attestation on internal control over financial reporting from their independent auditor.
- The amendments also would increase the public float threshold for exiting accelerated status to $60 million from $50 million and for exiting large accelerated status to $560 million from $500 million.
- Comments are due within 60 days of publication in the Federal Register.

Overview

The Securities and Exchange Commission (SEC) **proposed** amending the definitions of an accelerated filer and a large accelerated filer to exclude smaller reporting companies that have not yet begun to generate significant revenue.

In June 2018, the SEC expanded its definition of a smaller reporting company (SRC) to include, among others, issuers that have less than $100 million in annual revenue in their most recently completed year for which audited financial statements are available and less than $700 million in public float as of their annual measurement date.

The SEC is now proposing relief for this subset of SRCs to make them non-accelerated filers, with 45-day and 90-day deadlines to file their quarterly and annual reports, respectively. Consequently, as non-accelerated filers, these issuers would not be subject to the internal control attestation requirements of Section 404(b) of the Sarbanes-Oxley Act of 2002. The SEC estimates that the change would result in 539 more issuers being classified as non-accelerated filers.

Currently, all issuers with public float over $75 million are accelerated filers, with 40-day and 75-day reporting deadlines, without regard to their level of revenue. Further, accelerated filers are subject to the requirement to obtain an auditor's report on internal control over financial reporting (ICFR) each year, even if they get to make scaled disclosures as an SRC. Before the SEC expanded its SRC definition last year, all SRCs were non-accelerated filers and were exempt from these requirements.

The proposal also would increase the public float thresholds for companies exiting accelerated filer status and large accelerated filer status to make them consistent with the thresholds used in the revised definition of an SRC.

Key considerations

Changes to the accelerated filer and large accelerated filer definitions

Under the proposal, companies would qualify as non-accelerated filers if they qualify as an SRC and have revenue of less than $100 million in their most recently completed year for which audited financial statements are available.

The SEC isn't proposing to change the public float threshold for an accelerated filer. That is, a company with a public float of $75 million or more but less than $700 million would still be an accelerated filer, unless it qualifies as an SRC and has annual revenue below $100 million.

Thus, the SEC also isn't proposing to provide relief for all SRCs that qualify as accelerated filers. Issuers that qualify for SRC status under the public float test (i.e., they have a public float of less than $250 million but over $75 million) would still be accelerated filers if their annual revenue is $100 million or more. The SEC said it is proposing to limit the relief to issuers that it believes could benefit from the cost savings associated with non-accelerated filer status and redirect those savings into expanding their businesses.

The following table summarizes the proposed requirements:

Status	Public float	Annual revenues	Required to obtain auditor attestation over ICFR?
SRC and non-accelerated filer	Less than $75 million	No requirement	No
	$75 million to less than $700 million	Less than $100 million	No
SRC and accelerated filer	$75 million to less than $250 million	$100 million or more	Yes
Accelerated filer (not SRC)	$250 million to less than $700 million	$100 million or more	Yes
Large accelerated filer	$700 million and greater	No requirement	Yes

While foreign private issuers must file on domestic forms and use US GAAP in order to utilize the SRC accommodations if they qualify, the proposing release states the determination of filer status is based upon whether a foreign private issuer qualifies as an SRC under the SRC revenue test. Therefore, a foreign private issuer filing on Form 20-F or Form 40-F can still qualify as a non-accelerated filer if its annual revenues are less than $100 million and its public float is less than $700 million. The SEC estimates that 35 issuers filing on Form 20-F would become non-accelerated filers and, therefore, no longer be required to obtain an annual attestation on ICFR from their independent auditor.

How we see it

Independent audits of internal control of financial reporting support capital formation and investor protection, and have had a positive effect on investor confidence and market stability. The proposal would extend the exemption from the auditor attestation requirement for ICFR to a subset of small-cap companies that have not yet begun generating significant revenue, similar to a bill introduced in the Senate earlier this year.

Given that the proposal provides limited discussion of the benefits of an ICFR attestation for the population of issuers that would be exempted, feedback from investors and others through the comment process will be informative for the SEC. The proposal also would provide ongoing relief from Section 404(b) attestations for some issuers that exceed the five-year limit for emerging growth company status but have not yet achieved significant revenues.

Other changes

The proposal also would increase the thresholds for exiting accelerated status to $60 million from $50 million and for exiting large accelerated status to $560 million from $500 million (80% of the $75 million accelerated filer and $700 million large accelerated filer entrance thresholds) to make them consistent with the SRC definition.

In addition, it would add a revenue test to the transition thresholds as follows:

- An issuer with revenues above $100 million that qualifies as an SRC because of the public float test (i.e., has public float of less than $250 million) would become a non-accelerated filer if its revenue drops below $100 million.
- An issuer that has a public float and revenue over the SRC thresholds (i.e., greater than $250 million and $100 million, respectively) would become a non-accelerated filer and an SRC if its public float is below $560 million and its revenue drops below $80 million.[1]

Endnote:

[1] A large accelerated filer with public float between $560 million and $700 million that qualified as an SRC in the first year after the revised definition of an SRC became effective would qualify as a non-accelerated filer under the proposal if its revenue remained below $100 million.