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SEC Provides Further Relief for Smaller Public Companies

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The Securities and Exchange Commission (SEC) has issued two proposals (with a third expected shortly) to make reporting easier for smaller public companies. These came on the heels of three other recent SEC proposals ("June proposals") to make it easier and more cost effective for smaller public companies to raise capital (see Deloitte & Touche's July 3, 2007, *Heads Up*). All of these proposals (summarized in the table below) were issued in response to recommendations made by the SEC's Advisory Committee on Smaller Public Companies (the "Committee") in its April 2006 report.

While the proposals will provide some relief, the SEC did not act on the Committee's recommendation to exempt certain smaller companies from the internal control requirements of Sarbanes Oxley and to exempt other smaller companies from the requirement of having an auditor attest on internal controls. Interested in providing feedback on the proposals? See the comment letter deadlines below.

Topic	Highlight	Comment Deadline
	June Proposals	
Allowing Smaller Companies to Use Shelf Registration Statements (Forms S-3 and F-3)	Allows smaller companies to register securities before planning any specific offering and, once the registration statement is effective, to offer securities in one or more tranches without waiting for further SEC action.	August 27, 2007
Easing the Requirements for Unregistered Offerings (Rules 144 and 145)	Simplifies raising of capital by smaller companies in unregistered offerings.	September 4, 2007
Electronic Filing and Simplification of Form D	Allows electronic filing on the SEC's Web site of the notice of the sale of securities that are exempt from registration (Form D) and simplifies Form D.	September 7, 2007

Topic	Highlight	Comment Deadline
Current Proposals (covered in more detail below)		
Smaller Reporting Company Regulatory Relief and Simplification	Allows more companies to use the scaled SEC reporting disclosure rules created for the smallest public companies. Combines small business issuers and nonaccelerated filers into a single category entitled "smaller reporting companies" that generally have $75 million or less of public float.	September 17, 2007
Exemption of Compensatory Employee Stock Options from Registration	Exempts private companies from a current requirement to register employee stock options if they have over 500 option holders.	September 10, 2007
New Regulation D Limited Offering Exemption	Would establish an exemption from registration for sales of securities to "qualified purchasers" and permits the issuer to engage in limited advertising.	Proposal to be issued shortly

Smaller Reporting Company Regulatory Relief and Simplification

This proposal simplifies and consolidates into a single regulation the SEC reporting disclosure requirements for smaller companies. It also eliminates the S-B Forms that currently are not widely used for a variety of reasons, including a lack of acceptance in the marketplace.

The proposal combines small business issuers and nonaccelerated filers into a single category entitled "smaller reporting companies" that generally have $75 million or less of public float. If the proposal is adopted, these companies will be able to use the SEC's smaller company scaled reporting and disclosure requirements (up from companies with $25 million in public float today). The scaled reporting and disclosure requirements are summarized in the chart below. As a result of these changes, according to the SEC's estimate, approximately 42 percent of companies that file annual reports with the SEC would be able to use these disclosures. Companies that do not have a public float are eligible if they have revenues under $50 million annually. These ceilings will be adjusted for inflation every five years.

To provide maximum flexibility to smaller public companies, the proposal allows companies that qualify to choose either the larger company requirements or the smaller reporting company requirements "à la carte" (item by item).

Larger Company Requirement	Smaller Reporting Company Requirement
Audited balance sheet for **two** years, audited statement of income, cash flows and changes in stockholder equity for **three** years.	Audited balance sheet for **one** year, audited statement of income, cash flows and changes in stockholder equity for **two** years.
Five years of business development activities.	**Three** years of business development activities.
Five years of selected financial data and supplementary financial information.[1]	**Three** years of selected financial data and supplementary financial information.
Three years of MD&A.	**Two** years of MD&A.
Executive compensation disclosures for **five** executive officers. Executive compensation tables cover **five** years.	Executive compensation disclosures for **three** executive officers. Executive compensation tables cover **two** years.
Three years disclosure of certain related party transactions in excess of $120,000. Disclose policy and procedure for reviewing related person transactions.	**Two** years disclosure of certain related party transactions in excess of $120,000 or 1% of company's average year end total assets for the last two years.

1 Commonly referred to as Selected Quarterly Financial Data.

In lieu of using the S-B Forms, companies will now check a box on the cover of all filings indicating that they are eligible for smaller reporting company status. Smaller reporting companies would continue to benefit from the relief provided by the S-B forms (e.g., users of the S-B forms currently are not required to include a tabular disclosure of contractual obligations).

Editor's Note: Although the proposal incorporates most of the Committee's recommendations, the Committee had suggested that the scaled disclosures be made available to all companies with a market capitalization of less than $787 million, estimating that this threshold would result in 78.5 percent of public companies (which represents only 6 percent of total U.S. equity market capitalization) being able use the scaled disclosures. Because the proposed relief is limited to companies with a public float of $75 million, it will apply to fewer companies.

Exemption of Compensatory Employee Stock Options From Registration

This proposal exempts private companies from a current requirement to register employee stock options if the companies have over 500 option holders. The current rules only exempt grants of restricted stock to employees (not stock options). In addition, employee option holders would not be included in the number of security holders for the purpose of determining whether a company must be registered. For public companies, the proposal also exempts from registration options for which the underlying securities have already been registered.

Editor's Note: One of the primary reasons for the Committee's recommendation leading to this proposal was that several otherwise nonpublic companies had enough employee stock options outstanding to trigger the requirement to file periodic reports (i.e., Forms 10-K and 10-Q). This proposal allows qualifying companies to issue stock options to employees and become more "mature" before being subject to public reporting requirements.

New Regulation D Limited Offering Exemption

This proposal would establish an exemption from registration for sales of securities to "qualified purchasers" and permit the issuer to engage in limited advertising (currently no general solicitation or advertising is permitted). In addition, the proposal would increase the number of "accredited investors" (for which Regulation D already provides an exemption) by easing the qualification requirements. According to the SEC, as a result, the proposal will increase the pool of capital available to companies that engage in certain exempt offerings.

Editor's Note: Parts of this proposal will be attractive to all public companies that engage in private placement offerings, regardless of size. It would allow limited advertising and solicitation prior to determining that the investors are qualified, although investors must still be qualified before they can invest in the company. While the proposal removes a few federal-level impediments on private placement offerings, many states have modeled their rules after Regulation D as it stands today. These state "Blue Sky" laws will need to be revised for companies to take advantage of this proposal.

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