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# SEC Expands Qualifications for Nonaccelerated Filer Status

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## Introduction

On March 12, 2020, the SEC issued a [final rule](#)<sup>1</sup> that amends the eligibility criteria for nonaccelerated filer status to include issuers that qualify as smaller reporting companies (SRCs) with annual revenues of less than \$100 million and public float of less than \$700 million. The final rule is intended to promote capital formation while maintaining investor protection by expanding the number of issuers that are eligible to take advantage of certain reporting accommodations offered to nonaccelerated filers. The most significant of these accommodations is that nonaccelerated filers are not subject to the requirement under Section 404(b) of the Sarbanes-Oxley Act of 2002 (SOX) that an issuer obtain an audit report on internal control over financial reporting (ICFR) from its independent auditor.

In developing the final rule, the SEC considered feedback from constituents on its May 2019 [proposed rule](#).<sup>2</sup> The final rule is effective April 27, 2020, and may be applied to filings that are due on or after that effective date.

## Background

Before the SEC's [expansion](#)<sup>3</sup> of the definition of an SRC in September 2018, an issuer would not have been able to meet the SRC definition and also qualify as an accelerated filer. In response to suggestions from stakeholders, SEC Chairman Jay Clayton directed the staff to consider whether the accelerated filer definition also should be changed to more closely align

<sup>1</sup> SEC Final Rule Release No. 34-88365, *Amendments to the Accelerated Filer and Large Accelerated Filer Definitions*.

<sup>2</sup> SEC Proposed Rule Release No. 34-85814, *Amendments to the Accelerated Filer and Large Accelerated Filer Definitions*.

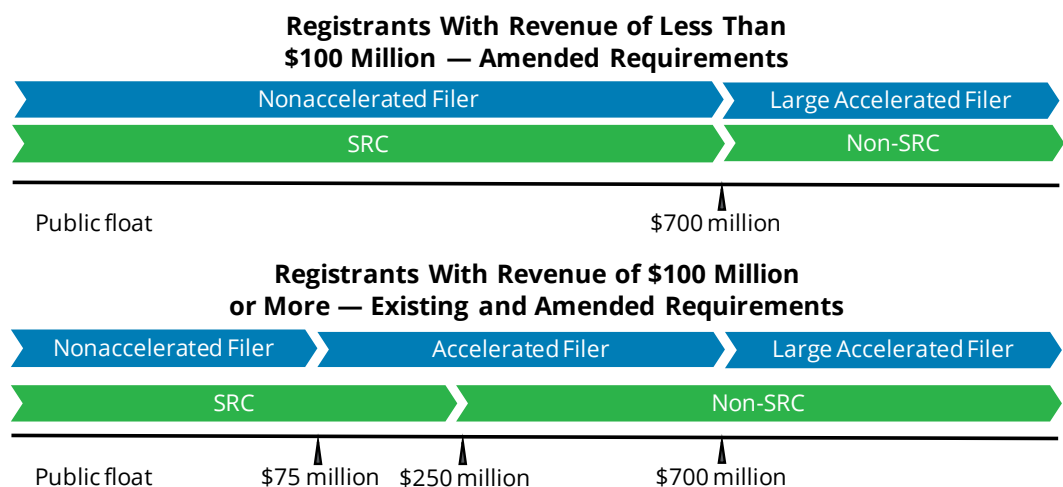
<sup>3</sup> SEC Final Rule Release No. 33-10513, *Smaller Reporting Company Definition*.

the two definitions. The final rule addresses those suggestions and more closely, although not completely, aligns an issuer's filing status determination with the amended SRC definition.

## Key Provisions of the Final Rule

The final rule amends the definitions of accelerated filer and large accelerated filer (under Rule 12b-2 of the Securities and Exchange Act of 1934) to exclude issuers that qualify as SRCs on the basis of a revenue test. Therefore, under the final rule, an issuer that qualifies as an SRC will also qualify as a nonaccelerated filer if it has (1) annual revenues of less than \$100 million in the most recent fiscal year for which audited financial statements are available and (2) a public float<sup>4</sup> of less than \$700 million as of the last business day of its second fiscal quarter (the "revenue test").

However, issuers that qualify as SRCs solely on the basis of a public float test (i.e., issuers with \$100 million or more of revenue but less than \$250 million of public float) will need to continue to separately evaluate the accelerated filer criteria<sup>5</sup> to determine their filing status, including the applicable public float thresholds (i.e., \$75 million or more to be considered an accelerated filer). While the final rule does not completely eliminate the overlap between SRCs and accelerated filers, it aligns the initial float assessment criteria for issuers with annual revenues under \$100 million. The chart<sup>6</sup> below illustrates the intersection between the revenue and public float requirements for an SRC and an accelerated filer under the existing and amended requirements.



The following table further summarizes the amended initial assessment criteria on the basis of public float and revenue levels in the context of the SOX Section 404(b) requirements:

Status	Amended Definition		Requirement
	Public Float	Annual Revenues	SOX Section 404(b)
SRC and nonaccelerated filer	Less than \$75 million	No limit	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

<sup>4</sup> Public float is the aggregate market value of the issuer's outstanding voting and nonvoting common stock held by nonaffiliates. It is calculated by multiplying the number of the company's voting and nonvoting common shares held by nonaffiliates by the market price.

<sup>5</sup> See [paragraphs 1340.1 and 1340.2](#) of the SEC Financial Reporting Manual for a full list of the criteria an issuer must meet, as assessed at the end of its fiscal year, to qualify as an accelerated filer or a large accelerated filer.

<sup>6</sup> The chart illustrates the amended definitions on the basis of public float. It is assumed in the chart that all other criteria under Rule 12b-2 have been met for an issuer to qualify as an accelerated filer or a large accelerated filer. The chart does not reflect requirements applicable to business development companies; for those requirements, see the [discussion](#) below.

### Example 1

Under the amended definition, an issuer with a December 31, 2020, fiscal year-end that has \$400 million of public float as of June 30, 2020, and \$95 million in annual revenues for the fiscal year ended December 31, 2019, will qualify as an SRC and will also be a nonaccelerated filer for the fiscal year ending December 31, 2020.

### Example 2

If the issuer's public float as of June 30, 2021, remains at \$400 million and its annual revenues for the fiscal year ending December 31, 2020, are \$105 million, the issuer will no longer qualify as an SRC or nonaccelerated filer because its public float exceeds \$75 million and it no longer has revenue less than \$100 million. Accordingly, when filing its annual report for the year ending December 31, 2021, the issuer must provide its independent auditor's report on the effectiveness of its ICFR and comply with the deadlines applicable to accelerated filers.

As a result of the final rule, certain SRCs will now qualify as nonaccelerated filers and will no longer be subject to auditor attestation of ICFR under SOX Section 404(b). However, the final rule does not relieve management of its obligation to assess ICFR nor does it relieve an independent auditor of its obligation to consider ICFR in the performance of its financial statement audit of an issuer. For example, in a financial statement audit, the auditor is required to identify and assess the risks of material misstatement. Thus, the auditor is required, in accordance with PCAOB AS 2110,<sup>7</sup> to "obtain a sufficient understanding of each component [of ICFR] to (a) identify the types of potential misstatements, (b) assess the factors that affect the risks of material misstatement, and (c) design further audit procedures." Obtaining such an understanding includes evaluating the design of the controls relevant to the audit and determining whether the controls have been implemented, but it does not include testing the operating effectiveness of those controls. In addition, the final rule does not affect other key SOX protections that do not depend on filer status, such as independent audit committee requirements, CEO and CFO certifications of financial reports, or the requirement that issuers continue to establish, maintain, and assess the effectiveness of their ICFR.

## Other Considerations

### Effective Date

As noted above, the final rule is effective April 27, 2020, and may be applied to annual reports due on or after that effective date. For example, if an issuer has a March 31, 2020, fiscal year-end and the due date for its annual report is after the final rule's effective date, the issuer may determine its filing status in accordance with the final rule. If the issuer qualifies as a nonaccelerated filer, it would not be required to provide an independent auditor's report on the effectiveness of ICFR, and it may use the reporting deadline applicable to nonaccelerated filers.

### Transition Thresholds

The final rule changes the public float criteria used to determine when an issuer will exit a filer status. To reduce the likelihood that issuers frequently change filer status, the SEC established lower criteria for exit than entry. Before the final rule's amendments, once an issuer became an accelerated filer or a large accelerated filer, it maintained that status until its public float fell below \$50 million or \$500 million, respectively. The final rule increases the public float transition threshold for a large accelerated filer or an accelerated filer to become a nonaccelerated filer from \$50 million to \$60 million, and for a large accelerated filer to become an accelerated filer from \$500 million to \$560 million (i.e., 80 percent of the initial qualification thresholds). In addition, the final rule allows an issuer to exit accelerated filer or

<sup>7</sup> Paragraph 18 of PCAOB Auditing Standard No. 2110, *Identifying and Assessing Risks of Material Misstatement*.

large accelerated filer status to become a nonaccelerated filer if it becomes eligible for SRC status under the revenue test at a revenue threshold of \$80 million (i.e., 80 percent of the initial qualification threshold).

## **Cover Page Update**

The final rule adds a checkbox to the cover pages of Forms 10-K, 20-F, and 40-F that all issuers must use to indicate whether the filing includes auditor attestation of ICFR.

## **Business Development Companies**

Business development companies<sup>8</sup> are excluded from the definitions of accelerated and large accelerated filer under an analogous revenue test in the final rule. Accordingly, while such companies are prohibited from being SRCs, they will be exempt from accelerated and large accelerated filer status if they have (1) a public float of less than \$700 million and (2) investment income (which includes income from dividends, interest on securities, and other income) of less than \$100 million. Business development companies with less than \$75 million in public float will continue to be nonaccelerated filers regardless of their investment income.

## **Foreign Private Issuers**

The final rule clarifies that the amendments apply to foreign private issuers (FPIs) that apply U.S. GAAP and file on domestic forms (i.e., Form 10-K and Form 10-Q). Issuers that qualify as FPIs and elect to use the FPI reporting regime (i.e., Form 20-F), however, are not eligible to be SRCs and therefore a revenue test would not be applicable for determining nonaccelerated filer status.

<sup>8</sup> The AICPA Audit and Accounting Guide *Investment Companies* defines a business development company as “a U.S. closed-end company that (1) operates for the purpose of making investments in certain securities specified in Section 55(a) of the 1940 Act and, with limited exceptions, makes available *significant managerial assistance* with respect to the issuers of such securities, and (2) has elected business development company status” in accordance with the 1940 Act.

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