

**SECURITIES AND EXCHANGE COMMISSION**

**17 CFR Parts 210, 229, 230, 239, 240, and 249**

**[Release Nos. 33-10513; 34-83550; File No. S7-12-16]**

**RIN 3235-AL90**

**SMALLER REPORTING COMPANY DEFINITION**

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Final rules.

**SUMMARY:** We are adopting amendments to the definition of “smaller reporting company” as used in our rules and regulations. The amendments expand the number of registrants that qualify as smaller reporting companies and are intended to reduce compliance costs for these registrants and promote capital formation, while maintaining appropriate investor protections. We are amending the definition of “smaller reporting company” to include registrants with a public float of less than \$250 million, as well as registrants with annual revenues of less than \$100 million for the previous year and either no public float or a public float of less than \$700 million. We also are amending other rules and forms in light of the new definition of “smaller reporting company,” including amendments to the definitions of “accelerated filer” and “large accelerated filer” to preserve the existing thresholds in those definitions. Qualifying as a “smaller reporting company” will no longer automatically make a registrant a non-accelerated filer. The Chairman, however, has directed the staff to formulate recommendations to the Commission for possible additional changes to the “accelerated filer” definition that, if adopted, would have the effect of reducing the number of registrants that qualify as accelerated filers.

**DATES:** The final rules are effective September 10, 2018.

**FOR FURTHER INFORMATION CONTACT:** Amy Reischauer or Jennifer Riegel, Office of Small Business Policy, Division of Corporation Finance, at (202) 551-3460, U.S. Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-3628.

**SUPPLEMENTARY INFORMATION:** We are adopting amendments to 17 CFR 230.405 (“Rule 405”) and Forms S-1,<sup>1</sup> S-3,<sup>2</sup> S-4,<sup>3</sup> S-8,<sup>4</sup> and S-11<sup>5</sup> under the Securities Act of 1933 (“Securities Act”);<sup>6</sup> 17 CFR 240.12b-2 (“Rule 12b-2”) and Forms 10,<sup>7</sup> 10-Q,<sup>8</sup> and 10-K<sup>9</sup> under the Securities Exchange Act of 1934 (“Exchange Act”);<sup>10</sup> 17 CFR 210.3-05 (“Rule 3-05” of Regulation S-X);<sup>11</sup> and 17 CFR 229.10(f) (“Item 10(f)” of Regulation S-K).<sup>12</sup>

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<sup>1</sup> 17 CFR 239.11.

<sup>2</sup> 17 CFR.239.13.

<sup>3</sup> 17 CFR 239.25.

<sup>4</sup> 17 CFR 239.16b.

<sup>5</sup> 17 CFR 239.18.

<sup>6</sup> 15 U.S.C. 77a *et seq.*

<sup>7</sup> 17 CFR 249.210.

<sup>8</sup> 17 CFR 249.308a.

<sup>9</sup> 17 CFR 249.310.

<sup>10</sup> 15 U.S.C. 78a *et seq.*

<sup>11</sup> 17 CFR 210.1-01 through 210.12-29.

<sup>12</sup> 17 CFR 229.10 through 229.1208.

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## I. Introduction

On June 27, 2016, the Commission proposed amendments that would increase the financial thresholds in the “smaller reporting company” (“SRC”) definition and would have the effect of expanding the number of companies that benefit from the scaled disclosure accommodations available to SRCs.<sup>13</sup> In developing final rules, we considered comment letters received in response to the Proposing Release,<sup>14</sup> as well as recommendations made by the Securities and Exchange Commission Advisory Committee on Small and Emerging Companies (“ACSEC”)<sup>15</sup> and the SEC Government-Business Forum on Small Business Capital Formation (“Small Business Forum”).<sup>16</sup> The Commission last revised the SRC definition in 2008.<sup>17</sup> Our

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<sup>13</sup> See Amendments to Smaller Reporting Company Definition, Release No. 33-10107 (Jun. 27, 2016) [81 FR 43130 (Jul. 1, 2016)] (“Proposing Release”). As the Commission noted in the Proposing Release, raising the financial thresholds in the SRC definition would be responsive to the Fixing America’s Surface Transportation Act of 2015 (“FAST Act”) because it would reduce the burden on the specified registrants by increasing the number of registrants eligible for scaled disclosure. See Pub. L. No. 114-94, 129 Stat. 1312 (2015).

<sup>14</sup> The comment letters received in response to the Proposing Release are available at <https://www.sec.gov/comments/s7-12-16/s71216.htm>.

<sup>15</sup> In September 2015 and March 2013, the ACSEC recommended revising the SRC definition to include registrants with a public float of up to \$250 million. The recommendations made by ACSEC in March 2013 also included a recommendation to revise the SRC definition for registrants that are unable to calculate their public float to include registrants with less than \$100 million in annual revenues. ACSEC Recommendations about Expanding Simplified Disclosure for Smaller Issuers (Sept. 23, 2015), available at <https://www.sec.gov/info/smallbus/acsec/acsec-recommendations-expanding-simplified-disclosure-for-smaller-issuers.pdf> and ACSEC Recommendations Regarding Disclosure and Other Requirements for Smaller Public Companies (Mar. 21, 2013), available at <https://www.sec.gov/info/smallbus/acsec/acsec-recommendation-032113-smaller-public-co-ltr.pdf>. Both of these recommendations also included a recommendation that the Commission revise the “accelerated filer” definition to include registrants with a public float of \$250 million or more, but less than \$700 million. The accelerated filer definition currently includes registrants with a public float of \$75 million or more, but less than \$700 million. See Exchange Act Rule 12b-2. See Section II.C for a discussion of the accelerated filer definition.

<sup>16</sup> The 2017 Small Business Forum recommended that the SRC definition be revised to include registrants with a public float of less than \$250 million or registrants with annual revenues of less than \$100 million, excluding large accelerated filers. See Final Report of the 2017 SEC Government Business Forum on Small Business Capital Formation (Mar. 2018), available at <https://www.sec.gov/files/gbfor36.pdf>. Registrants with a public float of \$700 million or more generally qualify as large accelerated filers. See Exchange Act Rule 12b-2. Prior Small Business Forums made the same or similar recommendations. Final Small Business Forum reports are available at <https://www.sec.gov/info/smallbus/sbforumreps.htm>. Information about the Small Business Forum is available at <http://www.sec.gov/info/smallbus/sbforum.shtml>. These recommendations also included a recommendation that the Commission revise the “accelerated filer” definition consistent with the recommended changes to the SRC definition. See Section II.C for a discussion of the accelerated filer definition.

amendments reflect the need to solicit input and retrospectively review our rules in order to determine whether they are outdated or are not functioning as intended. Today, we are amending the SRC definition in an effort to promote capital formation and reduce compliance costs for specified registrants by expanding the number of registrants that are eligible to provide scaled disclosure while maintaining appropriate investor protections.

We are adopting the amendments generally as proposed with two changes. As proposed, we are amending the SRC definition to include registrants with a public float of less than \$250 million, as well as registrants with annual revenues of less than \$100 million for the previous year and no public float. In a change from the proposal, the SRC definition in the final rules also includes registrants with annual revenues of less than \$100 million for the previous year and a public float of less than \$700 million. Specifically, we are amending Securities Act Rule 405, Exchange Act Rule 12b-2, and Item 10(f) of Regulation S-K to effect these changes. In another change from the proposal, we are amending Rule 3-05(b)(2)(iv) of Regulation S-X to increase the revenue threshold under which certain acquirers may omit the earliest of the three fiscal years of audited financial statements of certain targets. Finally, we are adopting amendments to the “accelerated filer” and “large accelerated filer” definitions in Exchange Act Rule 12b-2, as proposed, to preserve the application of the current public float thresholds in those definitions.<sup>18</sup> The Chairman, however, has directed the staff to formulate recommendations to the Commission for possible additional changes to the “accelerated filer” definition that, if adopted, would have

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<sup>17</sup> See Smaller Reporting Company Regulatory Relief and Simplification, Release No. 33-8876 (Dec. 19, 2007) [73 FR 934 (Jan. 4, 2008)] (“SRC Adopting Release”).

<sup>18</sup> The definitions of accelerated filer and large accelerated filer are based on public float, but currently contain a provision excluding registrants that are eligible to use the SRC requirements in Regulation S-K for their annual and quarterly reports. As a result, raising the SRC public float threshold without eliminating that provision effectively would raise the accelerated filer public float threshold. See Section II.C for a discussion of the amendments to the accelerated filer and large accelerated filer definitions.

the effect of reducing the number of registrants that qualify as accelerated filers in order to promote capital formation by reducing compliance costs for certain registrants, while maintaining appropriate investor protections. As part of the staff’s consideration of possible recommended amendments, the Chairman has directed the staff to consider, among other things, the historical and current relationship between the SRC and “accelerated filer” definitions. The staff has begun work to prepare these recommendations.

Consistent with the proposal, we are not amending any of the scaled disclosure accommodations available to SRCs in Regulation S-K and Regulation S-X.<sup>19</sup> SRCs may comply with the scaled disclosure requirements available to them on an item-by-item basis.<sup>20</sup> The following table summarizes these scaled disclosure accommodations.<sup>21</sup>

<b>Regulation S-K</b>	
<b>Item</b>	<b>Scaled Disclosure Accommodation</b>
101 – Description of Business	May satisfy disclosure obligations by describing the development of the registrant’s business during the last three years rather than five years. Business development description requirements are less detailed than disclosure requirements for non-SRCs.
201 – Market Price of and Dividends on the Registrant’s Common Equity and Related	Stock performance graph not required.

<sup>19</sup> Several of these scaled disclosure accommodations, such as the scaled executive compensation disclosures under Item 402(l) through (r) of Regulation S-K [17 CFR 229.402(l) through (r)], are similar to the disclosure accommodations available to an emerging growth company (“EGC”). See Securities Act Rule 405 [17 CFR 230.405] and Exchange Act Rule 12b-2 [17 CFR 240.12b-2]. EGCs also are exempt from the Sarbanes-Oxley Act Section 404(b) auditor attestation of internal control over financial reporting. For a discussion of scaled disclosure accommodations available to EGCs, see Business and Financial Disclosure Required by Regulation S-K, Release No. 33-10064 (Apr. 13, 2016) [81 FR 23915 (April 22, 2016)] (“Regulation S-K Concept Release”).

<sup>20</sup> See SRC Adopting Release, 73 FR at 940. Where a disclosure requirement applicable to SRCs is more stringent than the corresponding requirement for non-SRCs, however, SRCs must comply with the more stringent standard. The SRC Adopting Release identified Item 404 of Regulation S-K [17 CFR 229.404] as the only instance in Regulation S-K in which the disclosure requirements applicable to SRCs could be more stringent.

<sup>21</sup> In addition to the accommodations itemized in the table, SRCs using Form S-1 may incorporate by reference information filed prior and subsequent to the effectiveness of the registration statement if they meet the eligibility requirements in General Instruction VII of Form S-1. See Item 12(b) of Form S-1; see also Simplification of Disclosure Requirements for Emerging Growth Companies and Forward Incorporation by Reference on Form S-1 for Smaller Reporting Companies, Release No. 33-10003 (Jan. 19, 2016) [81 FR 2743 (Jan. 19, 2016)].

<b>Regulation S-K</b>	
<b>Item</b>	<b>Scaled Disclosure Accommodation</b>
Stockholder Matters	
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”)	Two-year MD&A comparison rather than three-year comparison. Two year discussion of impact of inflation and changes in prices rather than three years. Tabular disclosure of contractual obligations not required.
305 – Quantitative and Qualitative Disclosures About Market Risk	Not required.
402 – Executive Compensation	Three named executive officers rather than five. Two years of summary compensation table information rather than three. Not required: <ul style="list-style-type: none"> <li>• Compensation discussion and analysis.</li> <li>• Grants of plan-based awards table.</li> <li>• Option exercises and stock vested table.</li> <li>• Pension benefits table.</li> <li>• Nonqualified deferred compensation table.</li> <li>• Disclosure of compensation policies and practices related to risk management.</li> <li>• Pay ratio disclosure.</li> </ul>
404 – Transactions With Related Persons, Promoters and Certain Control Persons <sup>22</sup>	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.

<sup>22</sup> Item 404 also contains the following *expanded* disclosure requirements applicable to SRCs: (1) rather than a flat \$120,000 disclosure threshold, the threshold is the lesser of \$120,000 or 1% of total assets, (2) disclosures are required about underwriting discounts and commissions where a related person is a principal underwriter or a controlling person or member of a firm that was or is going to be a principal underwriter, (3) disclosures are required about the issuer’s parent(s) and their basis of control, and (4) an additional year of Item 404 disclosure is required in filings other than registration statements.



<b>Regulation S-X</b>	
<b>Rule</b>	<b>Scaled Disclosure</b>
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.

## **II. Final Amendments**

### **A. Amendments to Smaller Reporting Company Definition**

We are adopting amendments to the SRC definition to expand the number of registrants that qualify as SRCs and thereby benefit from scaled disclosure requirements. These amendments will enable a registrant to qualify as a SRC based on a public float test or a revenue test.<sup>23</sup>

Under the final rules, SRCs generally<sup>24</sup> are registrants with:

- a public float of less than \$250 million;<sup>25</sup> or

<sup>23</sup> See Item 10(f)(1)(i) and (ii) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

<sup>24</sup> Consistent with the current definition, the SRC definition in the final rules specifically excludes investment companies, asset-backed issuers (as defined in Item 1101 of Regulation AB [17 CFR 229.1101]) and majority-owned subsidiaries of a parent that is not a SRC. See Item 10(f)(1) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2. Lower public float and revenue thresholds apply to registrants that determined that they did not qualify as SRCs in the prior year, but are eligible to transition to SRC status. See Item 10(f)(2)(iii) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2. See also Section II.A for a discussion of the amendments to these thresholds.

<sup>25</sup> Consistent with the current definition, public float is computed under the final rules by multiplying the aggregate worldwide number of shares of a registrant's voting and non-voting common equity held by non-affiliates by the

- annual revenues of less than \$100 million<sup>26</sup> and either no public float<sup>27</sup> or a public float of less than \$700 million.<sup>28</sup>

As proposed, the final rules increase the threshold for determining SRC status based on public float from \$75 million to \$250 million. A registrant that qualifies as a SRC under the public float test would qualify regardless of its revenues.<sup>29</sup> In a change from the proposal, the final rules will expand the SRC definition to include registrants with a public float of less than \$700 million, if they also have annual revenues of less than \$100 million.<sup>30</sup> The following table

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price at which the common equity was last sold, or the average of the bid and asked prices of common equity, in the principal market for the common equity. *See* Item 10(f)(1)(i) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2. The determination of public float is premised on the existence of a public trading market for the issuer’s equity securities. Therefore, an entity with equity securities outstanding but not trading in any public trading market would not be able to qualify on the basis of a public float test. In contrast to public float, market capitalization reflects the value of a registrant’s voting and non-voting common equity held by all holders, whether affiliates or non-affiliates.

A reporting registrant calculates its public float as of the last business day of its most recently completed second fiscal quarter. *See* Item 10(f)(2)(i) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2. A registrant filing its initial registration statement under the Securities Act or Exchange Act calculates its public float as of a date within 30 days of the date the registration statement is filed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates before the registration plus, in the case of a Securities Act registration statement, the number of such shares included in the registration statement by the estimated public offering price of the shares. *See* Item 10(f)(2)(ii)(A) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

<sup>26</sup> Consistent with the current definition, annual revenues are as of the most recently completed fiscal year for which audited financial statements are available. Item 10(f)(2)(i)(B) and (f)(2)(ii)(B) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

<sup>27</sup> *See* Item 10(f)(1)(ii)(A) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2. A registrant may have no public float because it has no public common equity outstanding or no market price for its common equity exists. Based on data compiled by our Division of Economic and Risk Analysis (“DERA”), in calendar year 2016, approximately 21.5% of registrants that qualified as SRCs (and 7.7% of all registrants) had no public float. The estimated number of registrants with no public float here and elsewhere in this release may be over-inclusive due to the difficulty of ascertaining this status based on data extracted from registrants’ filings. *See* note 137 for a discussion of the methodology used by the staff to obtain this data.

<sup>28</sup> *See* Item 10(f)(1)(ii)(B) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

<sup>29</sup> *See* Instruction to Paragraph (f) of Item 10 of Regulation S-K; Instruction to definition of “smaller reporting company” in Securities Act Rule 405; Instruction to definition of “smaller reporting company” in Exchange Act Rule 12b-2.

<sup>30</sup> *See* Item 10(f)(1)(ii)(B) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

summarizes the amendments to the SRC definition for a registrant making an initial determination under the amendments<sup>31</sup> or a current SRC seeking to continue to qualify.

<b>Criteria</b>	<b>Current Definition</b>	<b>Revised Definition</b>
Public Float	Public float of less than \$75 million	Public float of less than \$250 million
Revenues	Less than \$50 million of annual revenues and no public float	Less than \$100 million of annual revenues and <ul style="list-style-type: none"> <li>• no public float, or</li> <li>• public float of less than \$700 million</li> </ul>

Consistent with the current definition, and as proposed, under the final rules, a registrant that determines that it does not qualify as a SRC under the initial qualification thresholds will remain unqualified unless and until it determines that it meets one or more lower qualification thresholds. The subsequent qualification thresholds, set forth in the table below, are set at 80% of the initial qualification thresholds.<sup>32</sup>

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<sup>31</sup> For purposes of the first fiscal year ending after effectiveness of the amendments, a registrant will qualify as a SRC if it meets one of the initial qualification thresholds in the revised definition as of the date it is required to measure its public float or revenues (the “measurement date”), even if such registrant previously did not qualify as a SRC. *See* Item 10(f)(2)(i) and (ii) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2 for additional information about the measurement date. For example, a registrant with a September 30 fiscal year end that previously was not a SRC and that had a public float of \$220 million as of March 30, 2018 (the last business day of its most recently completed second quarter) will qualify as a SRC for the fiscal year ending September 30, 2018.

<sup>32</sup> *See* Item 10(f)(2)(iii) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

Criteria <sup>33</sup>	Current Definition	Revised Definition
Public Float	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 <sup>34</sup>
Revenues	Less than \$40 million of annual revenues and no public float	Less than \$80 million of annual revenues, if it previously had \$100 million or more of annual revenues; and Less than \$560 million of public float, if it previously had \$700 million or more of public float.

## 1. Public Float Test

### a. Proposed Amendments

As proposed, a registrant with a public float of less than \$250 million would qualify as a SRC.<sup>35</sup> Consistent with the current definition, the Commission proposed that once a registrant does not qualify as a SRC,<sup>36</sup> it would remain unqualified until its public float falls below another, lower threshold. Specifically, the Commission proposed amending the rules to provide that a registrant that previously did *not* qualify as a SRC would qualify as a SRC if it has a public float of less than \$200 million as of its most recently completed second fiscal quarter.<sup>37</sup>

<sup>33</sup> A registrant that does not qualify as a SRC may subsequently seek to qualify under either test.

<sup>34</sup> A registrant that previously was not a SRC that subsequently qualifies based on a public float of less than \$200 million will qualify as a SRC regardless of its revenues. See Instruction to Paragraph (f) of Item 10 of Regulation S-K; Instruction to definition of “smaller reporting company” in Securities Act Rule 405; Instruction to definition of “smaller reporting company” in Exchange Act Rule 12b-2.

<sup>35</sup> See Proposed Item 10(f)(1)(i) and (ii) of Regulation S-K; Proposed Securities Act Rule 405; Proposed Exchange Act Rule 12b-2.

<sup>36</sup> This applies either upon an initial determination in the case of registrants filing an initial registration statement, or as of an annual determination in the case of reporting registrants.

<sup>37</sup> The proposed \$200 million subsequent qualification threshold represents 80% of the proposed \$250 million initial qualification threshold. Under the current definition, a registrant that previously determined that it did not qualify as a SRC because its public float exceeded the current \$75 million threshold may qualify based on a subsequent determination if it has a public float of less than \$50 million. That registrant would then remain a SRC until its public float again exceeded \$75 million. Consistent with the current definition, under the proposed definition, a registrant that subsequently qualifies under the \$200 million public float threshold would remain qualified until its public float exceeds \$250 million.

## **b. Comments**

Most commenters addressed the overall costs and benefits of expanding the pool of registrants eligible for SRC status. Many of these commenters expressed general support for the proposed amendments to the SRC definition.<sup>38</sup> Several of these commenters stated that the proposed definition appropriately considers the objectives of capital formation and investor protection<sup>39</sup> and promotes capital formation or liquidity for smaller registrants.<sup>40</sup>

On the other hand, three commenters generally opposed the proposed amendments to the SRC definition or generally opposed accommodations based on company size.<sup>41</sup> One of these commenters stated that the accommodations for SRCs exist solely for the expedience of issuers and must be balanced against the cost to market participants who have less information from which to draw conclusions.<sup>42</sup> Another of these commenters stated that it was concerned that the scaled disclosure regime for SRCs may prevent investors from receiving all of the material

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<sup>38</sup> See Letter from Acorda Therapeutics, Inc. et al, August 23, 2016 (“Acorda, et al”); Letter from Advanced Medical Technology Association, August 20, 2016 (“AMTA”); Letter from Biotechnology Innovation Organization, August 30, 2016 (“BIO”); Letter from BDO USA, LLP, August 29, 2016 (“BDO”); Letter from Center for Audit Quality and Counsel of Institutional Investors, August 30, 2016 (“CAQ/CII”); Letter from CONNECT, August 4, 2016 (“CONNECT”); Letter from Corporate Governance Coalition for Investor Value, August 30, 2016 (“Coalition”); Letter from Independent Community Bankers of America, August 29, 2016 (“ICBA”); Letter from MidSouth Bancorp, Inc., August 24, 2016 (“MidSouth”); Letter from Nasdaq, August 30, 2016 (“Nasdaq”); Letter from NYSE Group, July 25, 2016 (“NYSE”); Letter from National Venture Capital Association, August 25, 2016 (“NVCA”); Letter from Seneca Foods Corporation, August 2, 2016 (“Seneca”); and Letter from The Small Business Financial and Regulatory Affairs Committee of the Institute of Management Accountants, August 24, 2016 (“IMA”).

<sup>39</sup> See AMTA; BDO; BIO; Coalition; ICBA.

<sup>40</sup> See AMTA; BDO; BIO; Coalition; ICBA; NVCA; and NYSE. See also CONNECT (supporting the proposal to amend the SRC definition to encompass a wider range of emerging businesses for which regulatory costs present a significant burden to growth).

<sup>41</sup> See Letter from Cable Car Capital LLC, June 28, 2016 (“Cable Car”); Letter from CFA Institute, August 30, 2016 (“CFA Institute”); Letter from Ernst & Young LLP, September 8, 2016 (“EY”).

<sup>42</sup> See Cable Car.

information needed to conduct a thorough analysis.<sup>43</sup> This commenter also noted that allowing different sized entities to use different disclosure regimes would signal to investors that the entities lack comparable quality.<sup>44</sup> The third commenter recommended that the Commission consider adopting disclosure objectives that would mitigate the need to scale disclosure requirements based on the size or nature of a reporting entity.<sup>45</sup>

Two commenters stated that the proposed amendments would potentially provide only marginal cost savings.<sup>46</sup> One of these commenters did not support the proposal and instead encouraged the Commission to continue its review of scaled disclosure to determine which disclosures are repetitive and should be deleted and which should be retained.<sup>47</sup> The other commenter stated that the proposed change and the resulting reduced disclosure requirements for additional registrants would have a minimal effect on its annual compliance costs.<sup>48</sup>

Many commenters expressed support for the proposed increases in both the public float and revenue thresholds.<sup>49</sup> One commenter supported the amendments and viewed them as an acknowledgement that the current public float threshold is overly restrictive.<sup>50</sup> Another

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<sup>43</sup> See CFA Institute (noting that “the pension benefits table and a disclosure of compensation policies and practices related to risk management (both of which can be deleted under scaled disclosure) are more vital than certain other disclosures”).

<sup>44</sup> See CFA Institute.

<sup>45</sup> See EY (noting that it “previously recommended that the Commission consider adopting disclosure objectives that would mitigate the need for scaling disclosure requirements based on the size or nature of a reporting entity” and citing to its letter dated July 21, 2016 responding to the SEC’s concept release on business and financial disclosures required by Regulation S-K (Release No. 33-10064; File No. S7-06-16)).

<sup>46</sup> See CFA Institute; and Seneca.

<sup>47</sup> See CFA Institute.

<sup>48</sup> See Seneca.

<sup>49</sup> See Acorda et al; AMTA; BDO; BIO; CAQ/CII; CONNECT; Coalition; ICBA; MidSouth; Nasdaq; NVCA; NYSE; Seneca; and IMA.

<sup>50</sup> See Letter from Council of State Bioscience Associations, August 26, 2016 (“CSBA”) (stating that the Commission should similarly reform the accelerated filer definition and institute an alternative revenue test for both the SRC and accelerated filer definitions).

commenter specifically stated that it supported the proposed approach to adjusting the thresholds rather than simply relying on inflation adjustments.<sup>51</sup>

Two commenters recommended that the Commission review the SRC definition periodically to determine whether the thresholds being used remain appropriate.<sup>52</sup> One of these commenters specifically recommended that the Commission revisit the thresholds after three years.<sup>53</sup>

### **c. Final Amendments**

After considering the comments received, as well as the recommendations made by the ACSEC<sup>54</sup> and the Small Business Forum,<sup>55</sup> consistent with the proposal, we are adopting amendments to the SRC definition that will permit registrants with a public float of less than \$250 million to qualify as SRCs.<sup>56</sup> As is the case with the current definition, once a registrant determines that it does not qualify as a SRC under the applicable thresholds,<sup>57</sup> it will not subsequently qualify until its public float falls below another, lower threshold, set at 80% of the initial qualification threshold. While we did not receive any comments on the subsequent qualification thresholds, we continue to believe that these thresholds are necessary to avoid situations in which registrants frequently enter and exit SRC status due to small fluctuations in their public float and that the thresholds do not impose an undue burden on registrants seeking to qualify for SRC status. Accordingly, we are amending the rules to permit a registrant that

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<sup>51</sup> See NYSE.

<sup>52</sup> See CFA Institute; and Letter from Kermit Kubitz, August 31, 2016 (“Kubitz”).

<sup>53</sup> See Kubitz.

<sup>54</sup> See note 15.

<sup>55</sup> See note 16.

<sup>56</sup> See Item 10(f)(1)(i) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

<sup>57</sup> This applies either upon an initial determination in the case of registrants filing an initial registration statement, or as of an annual determination in the case of reporting registrants.

previously did not qualify as a SRC because its public float was \$250 million or more to qualify as a SRC if it has a public float of less than \$200 million, regardless of its revenues.<sup>58</sup>

We are not revising the method of calculating public float, as suggested by one commenter.<sup>59</sup> The staff is not aware of significant incidence of manipulation or stock price volatility affecting qualification under the public float test. In addition, the method of calculating public float is consistent with the existing rules and with the method of determining eligibility to use Form S-3 or Form F-3 to register a primary offering.<sup>60</sup> This consistency will avoid additional burdens or confusion for registrants and investors that may result if registrants were required to calculate their public float in one manner for determining SRC status and in another manner for Form S-3 or Form F-3 eligibility.

We believe that these amendments will promote capital formation through a modest reduction in compliance costs for newly eligible SRCs while maintaining appropriate investor protections.<sup>61</sup> In 2016, approximately 28% of registrants had less than \$75 million in public float,<sup>62</sup> compared to approximately 42% of registrants when the SRC definition was established.<sup>63</sup>

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<sup>58</sup> See Item 10(f)(2)(iii)(A) and Instruction to Paragraph (f) of Item 10 of Regulation S-K; Securities Act Rule 405 and Instruction to definition of “smaller reporting company” in Securities Act Rule 405; Exchange Act Rule 12b-2 and Instruction to definition of “smaller reporting company” in Exchange Act Rule 12b-2. Consistent with the current definition, under the amended definition, a registrant that subsequently qualifies under the \$200 million public float threshold would remain qualified until its public float exceeds \$250 million.

<sup>59</sup> See Letter from Paul W. Zeller, July 18, 2016 (“Zeller”) (suggesting that the Commission, in the calculation of public float, adopt a revenue test for thinly traded registrants to address price manipulation and volatility concerns).

<sup>60</sup> See Instructions I.B.1 and I.B.6 of Form S-3; Instructions I.B.1 and I.B.5 of Form F-3. Certain newly eligible SRCs under the new definition will continue to be eligible to rely on Instruction I.B.1 of Form S-3 and Form F-3 to register primary offerings.

<sup>61</sup> See Section IV.B.

<sup>62</sup> Based on public float values disclosed by registrants in their Form 10-K filings, 2,072, or 28.0%, of the 7,395 registrants that filed a Form 10-K in 2016 reported having a public float of less than \$75 million.

<sup>63</sup> Approximately 4,976, or 41.8%, of the 11,898 registrants that filed Exchange Act annual reports in 2006 had a public float of less than \$75 million. See SRC Adopting Release. The release cites data from the Commission’s EDGAR filing system and Thomson Financial (“Datastream”). The Datastream data included all registered



Increasing the public float threshold to \$250 million would have resulted in approximately 39% of registrants qualifying as SRCs in 2016 based on their public float.<sup>64</sup>

We believe the existing scaled disclosure accommodations have reduced compliance costs for SRCs.<sup>65</sup> These amendments will extend those benefits to a broader pool of registrants, consistent with the intent of the Commission when it adopted the SRC definition in 2007.<sup>66</sup>

Although the amendments will permit a broader group of registrants to make scaled disclosure to their investors, we do not believe that this scaling of disclosure will detract substantially from the investor protection objectives of our disclosure regime in light of the other protections available under current law and regulations. First, the additional registrants that will qualify for scaled disclosure, like all registrants, will remain liable for their disclosures<sup>67</sup> and, in addition to the disclosure expressly required by the rules, will continue to be required to provide such further material information, if any, as may be necessary to make any required statements, in the light of the circumstances under which they are made, not misleading.<sup>68</sup> Moreover, their disclosure also will continue to be subject to the Division of Corporation Finance's filing review process. These measures of investor protection will remain unchanged.

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public firms trading on the New York Stock Exchange, the American Stock Exchange, the Nasdaq, the Over-the-Counter Bulletin Board and the Pink Sheets and excluded closed end funds, exchange traded funds, American depository receipts and direct foreign listings.

<sup>64</sup> Based on public float values disclosed by registrants in their Form 10-K filings, 2,851, or 38.6%, of the 7,395 registrants that filed a Form 10-K in 2016 reported having a public float of less than \$250 million.

<sup>65</sup> See Section IV.B.3.a.

<sup>66</sup> See SRC Adopting Release, 73 FR at 934 and 942 (stating that the Commission was “adopting amendments to its disclosure and reporting requirements...to expand the number of companies that qualify for its scaled disclosure requirements for smaller reporting companies;” and “[w]e believe this standard is appropriately scaled in that it reduces costs to smaller companies caused by unnecessary information requirements, consistent with investor protection.”).

<sup>67</sup> See, e.g., Sections 11, 12, and 17 of the Securities Act, Sections 10(b) and 18 of the Exchange Act, and Exchange Act Rule 10b-5 [17 CFR 240.10b-5].

<sup>68</sup> See Securities Act Rule 408 [17 CFR 230.408] and Exchange Act Rule 12b-20 [17 CFR 240.12b-20].

## **2. Revenue Test**

### **a. Proposed Amendments**

As proposed, a registrant with no public float would qualify as a SRC if it had annual revenues of less than \$100 million during its most recently completed fiscal year.<sup>69</sup> Consistent with the current definition, the Commission proposed that once a registrant determines that it does not qualify as a SRC,<sup>70</sup> it would not subsequently qualify until its revenues fall below another, lower threshold. Specifically the Commission proposed amending the rules to provide that a registrant with no public float that previously determined that it did not qualify as a SRC would qualify as a SRC if it had annual revenues of less than \$80 million as of the relevant measurement date.<sup>71</sup> The proposed \$80 million subsequent qualification threshold would maintain the 80% ratio that exists between the \$50 million initial qualification threshold and \$40 million subsequent qualification threshold in the current SRC definition.

The Proposing Release noted that the 2015 Small Business Forum recommended that the SRC definition be revised to include, in addition to registrants with a public float of less than \$250 million, registrants with a public float of less than \$700 million and annual revenues of less than \$100 million.<sup>72</sup> The Proposing Release also solicited comment on whether the Commission should revise the SRC definition to include an alternative revenue test.

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<sup>69</sup> See Proposed Item 10(f)(1)(ii)(A) of Regulation S-K; Proposed Securities Act Rule 405; Proposed Exchange Act Rule 12b-2.

<sup>70</sup> This applies either upon an initial determination in the case of registrants filing an initial registration statement, or as of an annual determination in the case of reporting registrants.

<sup>71</sup> Under the current definition, a registrant that previously determined that it did not qualify as a SRC because it had no public float and its revenues exceeded the current \$50 million threshold may qualify based on a subsequent determination if it had annual revenues of less than \$40 million. That registrant would then remain a SRC until its revenues exceeded \$50 million. Consistent with the current definition, under the proposed definition, a registrant with no public float that subsequently qualifies under the \$80 million revenue threshold would remain qualified until its revenue exceeds \$100 million.

<sup>72</sup> See Proposing Release at text accompanying note 22.

## **b. Comments**

Many commenters recommended that the Commission add a revenue test to the SRC definition for companies with a public float.<sup>73</sup> Several commenters stated that businesses below \$100 million in revenue are viewed by reasonable observers as “small.”<sup>74</sup> One commenter believed that a revenue test would stimulate innovation and drive business growth.<sup>75</sup> Another commenter stated that a revenue test would ensure that pre-revenue companies are not “forced to divert investment funds...from science to compliance.”<sup>76</sup> Another commenter supported an alternative revenue test for highly valued pre-revenue companies “to avoid stifling the advancement” of these companies with costly compliance.<sup>77</sup> Two commenters suggested that we adopt a revenue test without a limitation on the public float or market capitalization of the company.<sup>78</sup> Another two commenters specifically recommended that the Commission adopt a definition based on revenues of less than \$100 million and a public float of less than \$700 million, as recommended by the Small Business Forum.<sup>79</sup>

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<sup>73</sup> See Acorda, et al (recommending a revenue test, stating that public float is largely a marker of future value but paints an inaccurate picture of small businesses in the present); AMTA; BIO (stating that the Commission should move away from its reliance on public float as the ultimate arbiter of company size); Letter from Calithera Biosciences, August 8, 2016 (“Calithera”); CONNECT; CSBA; Nasdaq (recommending a well-crafted revenue only threshold); NYSE (recommending a simple revenue test without a limitation on market capitalization); and Zeller (recommending a revenue test for any issuers that are thinly traded). See also Section II.A.1.b for a discussion of comments addressing the overall costs and benefits of expanding the pool of registrants eligible for SRC status, including the proposed revision to expand the revenue threshold for registrants with no public float.

<sup>74</sup> See Acorda, et al; BIO; and Calithera.

<sup>75</sup> See BIO (stating that pre-revenue small businesses should remain focused on innovation and do not have the capital to pay for expensive compliance requirements, and therefore allowing them to qualify as SRCs until they generate revenue would stimulate innovation and drive business growth).

<sup>76</sup> See Acorda, et al.

<sup>77</sup> See AMTA.

<sup>78</sup> See NYSE; and Nasdaq.

<sup>79</sup> See BIO; and Calithera.

### c. Final Amendments

After considering the comments received as well as the recommendations made by the ACSEC<sup>80</sup> and the Small Business Forum,<sup>81</sup> we are adopting the proposed amendments to the revenue test of the SRC definition and expanding the revenue test to include certain registrants with a public float. The definition in the final rules will include, in addition to registrants with a public float of less than \$250 million, registrants with annual revenues of less than \$100 million during their most recently completed fiscal year and either no public float (calculated as discussed in Section II.A.1) or a public float of less than \$700 million.<sup>82</sup> We are persuaded by commenters' suggestions that it is appropriate to provide a measure by which a registrant with a public float but limited revenues may qualify as a SRC.<sup>83</sup> This amended revenue test expands the proposed revenue threshold for companies with no public float to permit registrants with a public float that is less than \$700 million to qualify based on their revenues. The \$700 million public float threshold included in this amended revenue test was recommended by two commenters<sup>84</sup> and the Small Business Forum.<sup>85</sup> This change from the proposal permits some additional registrants to

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<sup>80</sup> See note 15.

<sup>81</sup> See note 16.

<sup>82</sup> See Item 10(f)(1)(ii) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2. Under the public float test discussed in Section II.A.1., a registrant with public float of less than \$250 million will qualify as a SRC regardless of its revenues. See Instruction to Paragraph (f) of Item 10 of Regulation S-K; Instruction to definition of "smaller reporting company" in Securities Act Rule 405; Instruction to definition of "smaller reporting company" in Exchange Act Rule 12b-2.

<sup>83</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; and CSBA.

<sup>84</sup> See BIO and Calithera.

<sup>85</sup> See note 16. In 2016 and 2017, the Small Business Forum recommended that the SRC definition be revised to include registrants with a public float of less than \$250 million or registrants with annual revenues of less than \$100 million, excluding large accelerated filers. Registrants with a public float of \$700 million or more generally qualify as large accelerated filers. See Exchange Act Rule 12b-2. In prior years, the Small Business Forum recommended that the Commission revise the SRC definition to include registrants with a public float of less than \$250 million or registrants with a public float of less than \$700 million and annual revenues of less than \$100 million. See, e.g., Final Report of the 2015 SEC Government Business Forum on Small Business Capital Formation (Apr. 2016), available at <https://www.sec.gov/info/smallbus/gbfor34.pdf>.

qualify as SRCs,<sup>86</sup> and we believe that these low-revenue registrants would benefit from the cost savings of scaled disclosure accommodations and could redirect those savings into growing their businesses without significantly detracting from investor protections. For example, these registrants will remain liable for their disclosures, will continue to be required to provide all material information necessary to make any required statements not misleading, and will continue to be subject to the Division of Corporation Finance's filing review process.

The amended revenue test that we are adopting is consistent with the position expressed by several commenters<sup>87</sup> that it is not necessary to subject capital-intensive, low-revenue registrants with larger public floats or market capitalizations to the same reporting requirements as registrants with larger public floats and more well-established, revenue-generating businesses. Although two commenters suggested that we adopt a revenue test without a limitation on the public float or market capitalization of the company,<sup>88</sup> we believe that it is appropriate to include a public float limitation because, as a registrant's business and public float grows, investors should benefit from greater disclosure. The additional information provided by the registrant in these circumstances will assist a growing investor base in making informed investment decisions and also should lead to a lower cost of capital for the business as it grows. In this way, the amended revenue test in the final rules will enable some additional capital-intensive, low-revenue registrants to benefit from the cost-savings of scaled reporting, while continuing to require larger registrants to comply with the disclosure requirements applicable to non-SRCs.

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<sup>86</sup> Excluding the 2,851 registrants that based on their 2016 data would qualify under the public float test described in Section II.A.1 and the 594 registrants that would qualify under the proposed no public float and less than \$100 million in annual revenues test, we estimate that this change would permit an additional 161 registrants to qualify as a SRC.

<sup>87</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; CSBA; NYSE; and Nasdaq.

<sup>88</sup> See NYSE; and Nasdaq.

In 2016, approximately 7.7% of registrants qualified as SRCs by having no public float and less than \$50 million in annual revenues.<sup>89</sup> The number of registrants that would qualify as SRCs would have increased by 26, or 0.4%, under the new \$100 million annual revenue threshold for registrants with no public float.<sup>90</sup> Expanding the definition further to include registrants with annual revenues of less than \$100 million and public float of less than \$700 million would have increased the number of eligible registrants by an additional 161, or 2.2%.<sup>91</sup>

Under the current definition, and as proposed, once a registrant with no public float determines that it does not qualify as a SRC,<sup>92</sup> it cannot subsequently qualify based on revenues until its revenues fall below another, lower threshold. As discussed above with respect to the public float test, while we did not receive any comments on the subsequent qualification thresholds, we believe that a separate, lower revenue threshold for these registrants helps to avoid situations in which registrants enter and exit SRC status due to small fluctuations in their revenues and does not impose an undue burden on registrants seeking to qualify for SRC status. Therefore, consistent with the proposal, once an issuer with no public float determines that it does not qualify for SRC status because its annual revenues exceeded \$100 million, it will remain

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<sup>89</sup> Based on public float values and revenues disclosed by registrants in their Form 10-K filings in 2016, 568, or 7.7%, of the 7,395 registrants that filed a Form 10-K in 2016 reported having no public float and less than \$50 million in annual revenues.

<sup>90</sup> Based on public float values and revenues disclosed by registrants in their Form 10-K filings in 2016, 26, or 0.4%, of the 7,395 registrants that filed a Form 10-K in 2016 had no public float and \$50 million or more but less than \$100 million in annual revenues.

<sup>91</sup> Based on public float values and revenues disclosed by registrants in their Form 10-K filings in 2016, 161, or 2.2%, of the 7,395 registrants that filed a Form 10-K in 2016 had \$250 million or more but less than \$700 million of public float and less than \$100 million in annual revenues.

<sup>92</sup> This applies either upon an initial determination in the case of registrants filing an initial registration statement, or as of an annual determination in the case of reporting registrants.

unqualified unless and until its annual revenues are less than \$80 million as of the measurement date.<sup>93</sup>

Consistent with the 80% ratio we are adopting for the other subsequent qualification thresholds, under the amended revenue test, once a registrant with public float determines that it does not qualify as a SRC because it exceeds either or both of the \$100 million annual revenue and \$700 million public float thresholds, it will remain unqualified unless and until it meets a lower threshold for the criteria on which it previously failed to qualify (\$80 million of annual revenue and \$560 million of public float) and continues to meet any threshold it previously satisfied (\$100 million of annual revenue or \$700 million of public float).<sup>94</sup> By requiring that a registrant satisfy a lower threshold only with respect to a threshold it previously exceeded, we are attempting to strike a balance between avoiding situations in which registrants frequently enter and exit SRC status due to small fluctuations and not imposing an undue burden on registrants seeking to qualify for SRC status. A registrant that exceeded both the public float threshold and the revenue threshold, however, would not qualify unless and until it met both lower thresholds in order to avoid situations in which registrants enter and exit SRC status due to small fluctuations in either their revenues or public float. The table below sets forth the thresholds for qualification as of the respective measurement date under the amended revenue test after one or both thresholds have been exceeded:

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<sup>93</sup> See Item 10(f)(2)(iii)(B) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2. Consistent with the current definition, under the amended definition, a registrant with no public float that subsequently qualifies under the \$80 million revenue threshold remains qualified until its revenue exceeds \$100 million.

<sup>94</sup> *Id.* Consistent with the current definition, under the amended definition, a registrant that subsequently qualifies under the \$560 million public float threshold or \$80 million revenue threshold remains qualified until its public float exceeds \$700 million or its revenue exceeds \$100 million.

Prior Annual Revenues	Prior Public Float	
	None or less than \$700 million	\$700 million or more
Less than \$100 million	Neither threshold exceeded.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$100 million.
\$100 million or more	<b>Public float</b> None or less than \$700 million; and <b>Revenues</b> Less than \$80 million.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$80 million.

### B. Amendments to Rule 3-05(b)(2)(iv) of Regulation S-X

In the Proposing Release, the Commission asked whether, if the revenue threshold in the SRC definition is increased, the threshold in Rule 3-05 of Regulation S-X also should increase. Rule 3-05 of Regulation S-X provides the requirements for financial statements of businesses acquired or to be acquired in certain registration statements and current reports. Current paragraph (b)(2)(iv) allows certain registrants to omit such financial statements for the earliest of the three fiscal years required if the net revenues of the business to be acquired are less than \$50 million.<sup>95</sup> The \$50 million threshold is based on the revenue threshold in the SRC definition.<sup>96</sup>

<sup>95</sup> Rule 3-05(b)(2) sets forth the requirements for financial statements of an acquired business or to be acquired business to be provided other than when registering securities to be offered to the security holders of the business to be acquired.

<sup>96</sup> In 1996, the Commission revised Rule 3-05 to streamline the requirements for financial statements of significant business acquisitions in filings made under the Securities Act and the Exchange Act, stating:

“The threshold at which audited financial statements of an acquired business are required for three years, as required for the issuer itself (except for small business issuers), has been raised from 40% to 50% in recognition of the significant burden imposed by the lower threshold. In addition, consistent with the criteria for small business issuers, financial statements for periods preceding the most recent two fiscal years would not be required for acquired businesses reporting revenues below \$25 million.” *See Streamlining Disclosure Requirements Relating to Significant Business Acquisitions*. Release No. 33-7355 (Oct. 10, 1996) [61 FR 54509 (Oct. 18, 1996)] (“1996 Rule 3-05 Adopting Release”).

When the Commission adopted the SRC definition (which replaced the small business issuer definition) in 2007, it noted:



Two commenters recommended amending Rule 3-05 to increase the revenue threshold in paragraph (b)(2)(iv) to \$100 million to maintain the alignment between Rule 3-05 and the definition of a SRC.<sup>97</sup> One commenter noted that this alignment should be retained to “maintain the objective the Commission expressed when it adopted the 2007 S-X Rule 3-05 relief.”<sup>98</sup> The other commenter noted that this amendment would avoid having the financial statement requirements for a SRC-sized target company exceed those of a similarly sized registrant.<sup>99</sup>

Consistent with these comments, we are amending Rule 3-05 to increase the net revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X to \$100 million.<sup>100</sup> Given that the current \$50 million revenue threshold in Rule 3-05(b)(2)(iv) was based on the revenue threshold in the SRC definition, and in light of our decision to increase the revenue threshold in the SRC definition from \$50 million to \$100 million, we are raising the net revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X from \$50 million to \$100 million.

## **C. Amendments to Accelerated Filer and Large Accelerated Filer Definitions**

### **1. Proposed Amendments**

The Commission proposed amending the definitions of “accelerated filer” and “large accelerated filer” to remove the automatic exclusion from these definitions of any registrant that

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“Several comment letters noted that in light of the \$50 million in revenues threshold proposed for determining a company’s qualification as a SRC if a company is unable to calculate public float, the Commission should consider revising [Rule 3-05(b)(2)(iv)] to raise to \$50 million the \$25 million threshold currently used to limit to two the periods required for audited financial statements of an acquired business. The \$25 million threshold was based on the \$25 million in revenues standard in Regulation S-B that we are rescinding. We are amending this standard to increase the threshold to \$50 million in revenues, as suggested by the commenters.” *See SRC Adopting Release.*

<sup>97</sup> *See EY; and BDO.* No other commenters addressed whether to amend Rule 3-05 of Regulation S-X.

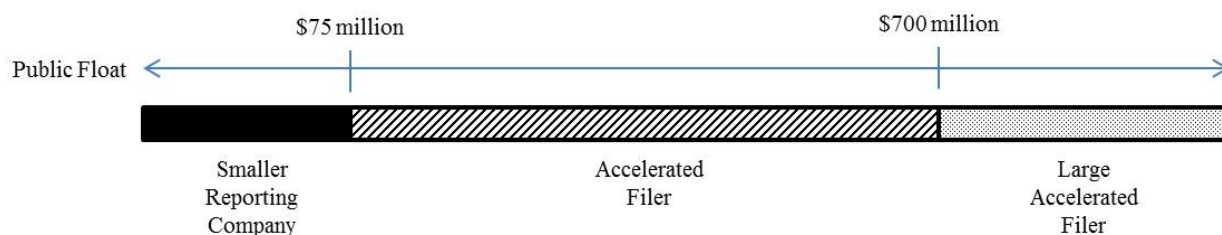
<sup>98</sup> *See EY; see also SRC Adopting Release.*

<sup>99</sup> *See BDO.*

<sup>100</sup> *See Rule 3-05(b)(2)(iv) of Regulation S-X.*

qualifies as an SRC<sup>101</sup> and solicited comment on a number of questions related to this issue.<sup>102</sup> Among other requirements,<sup>103</sup> being an accelerated filer or a large accelerated filer triggers the requirement contained in Section 404(b) of the Sarbanes-Oxley Act<sup>104</sup> to have the auditor provide an attestation report on internal control over financial reporting. Currently, the accelerated filer and large accelerated filer definitions include a provision that specifically excludes registrants that are eligible to use the SRC requirements under Regulation S-K for their annual and quarterly reports.<sup>105</sup> As a result, the existing public float threshold in the accelerated filer definition aligns with the current public float threshold in the SRC definition.<sup>106</sup>

**Figure 1: Current Definitions of SRC, Accelerated Filer, and Large Accelerated Filer**



<sup>101</sup> See Proposing Release, 81 FR at 43136.

<sup>102</sup> See Proposing Release, 81 FR at 43137. As discussed in the Proposing Release, the ACSEC and the Small Business Forum have recommended increasing the thresholds in both the SRC and the accelerated filer definitions. See notes 15 and 16.

<sup>103</sup> Accelerated and large accelerated filers are subject to accelerated periodic report filing deadlines. In addition, they must provide their internet address and disclosure regarding the availability of their filings required by Items 101(e)(3) and (4) of Regulation S-K [17 CFR 229.101(e)(3) and (4)], as well as disclosure required by Item 1B of Form 10-K about unresolved staff comments on their periodic or current reports.

<sup>104</sup> Pub. L. 107-204, Sec. 404(b) 116 Stat. 745 (2002).

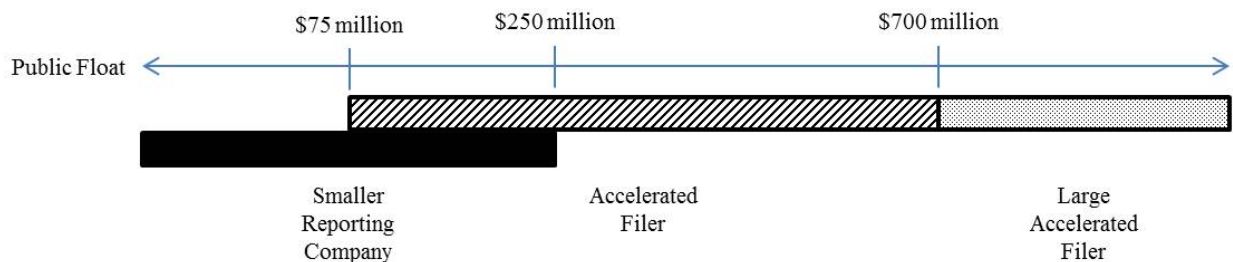
<sup>105</sup> Paragraphs (1)(iv) of the accelerated filer definition and (2)(iv) of the large accelerated filer definition in Exchange Act Rule 12b-2.

<sup>106</sup> The public float thresholds for exiting SRC status and entering accelerated filer status currently are both \$75 million, and the determinations are both made as of the last business day of a registrant's most recently completed second fiscal quarter for purposes of the following fiscal year.

Increasing the SRC public float threshold to \$250 million without eliminating the SRC provision from the accelerated filer definition would exclude from the definition of accelerated filer those registrants that are newly eligible to use the SRC disclosure requirements, keeping the thresholds for both definitions linked as they have been historically.

The Commission proposed to eliminate the provision in the accelerated filer definition that excludes SRCs to maintain the current thresholds at which registrants are subject to the accelerated filer disclosure and filing requirements. As a result, as illustrated in Figure 2, some registrants would qualify as both SRCs and accelerated filers.

**Figure 2: Proposed Definitions of SRC, Accelerated Filer and Large Accelerated Filer**



As discussed in the Proposing Release, the public float threshold for entering large accelerated filer status currently is \$700 million, so newly eligible SRCs under the proposed increased public float threshold of \$250 million would not include any registrants that currently qualify as large accelerated filers. Nevertheless, the Commission proposed to eliminate this provision because it currently does not capture any registrants, would not have captured any registrants under the proposed amendments, and could lead to confusion if retained.

## 2. Comments

Some commenters responded to the Commission’s solicitation of comment on this issue by supporting the elimination of the provisions in the accelerated filer and large accelerated filer

definitions that specifically exclude registrants that are eligible to use the SRC disclosure requirements for their annual or quarterly reports.<sup>107</sup> One commenter stated that it found no compelling argument to support what it sees as a weakening of investor protections, particularly in light of the 2011 Staff Section 404(b) Study<sup>108</sup> finding that accelerated filers subject to Section 404(b) had a lower restatement rate compared to non-accelerated filers not subject to Section 404(b).<sup>109</sup> Another commenter recommended that the Commission undertake a separate rulemaking before deciding whether to change the Section 404(b) requirements.<sup>110</sup> A third commenter recommended that the Commission provide more time for registrants with a public float of less than \$250 million to file their periodic reports.<sup>111</sup>

In contrast, many commenters responded to the Commission's solicitation of comment on this issue by recommending that the Commission increase the thresholds in the accelerated filer definition, consistent with the changes to the SRC definition.<sup>112</sup> Commenters recommended increasing the public float threshold in the accelerated filer definition to reduce compliance costs<sup>113</sup> and to maintain uniformity across our rules.<sup>114</sup> Many of these commenters stated that

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<sup>107</sup> See BDO; CAQ/CII; CFA Institute; Letter from Deloitte, August 23, 2016 ("Deloitte"); and EY.

<sup>108</sup> Study and Recommendations on Section 404(b) of the Sarbanes-Oxley Act of 2002 For Issuers With Public Float Between \$75 and \$250 Million (Apr. 2011), available at <https://www.sec.gov/news/studies/2011/404bfloat-study.pdf>.

<sup>109</sup> See CFA Institute, citing 2011 Staff Section 404(b) Study.

<sup>110</sup> See EY.

<sup>111</sup> See BDO.

<sup>112</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; Coalition; CSBA; ICBA; Letter from The Dixie Group, Inc., July 11, 2016 ("Dixie"); MidSouth; Nasdaq; NVCA; NYSE; and Seneca.

<sup>113</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; Coalition; CSBA; ICBA; Dixie; MidSouth; Nasdaq; NVCA; NYSE; and Seneca.

<sup>114</sup> See BIO (stating that uniformity alone is a sufficiently compelling argument to align the two definitions, that avoiding investor confusion is an important responsibility of the SEC, and that issuers and investors alike are used to having one standard for small company status); Coalition; Nasdaq; NVCA; and NYSE.

Section 404(b) is particularly costly for SRCs and emerging businesses<sup>115</sup> and that audit costs associated with Section 404(b) divert capital from core business needs.<sup>116</sup>

Several commenters addressed the costs associated with complying with the requirements of Section 404(b).<sup>117</sup> A few commenters stated that, for many growing biotechnology companies, the Section 404(b) audit represents over \$1 million of capital diversion.<sup>118</sup> One commenter indicated that Section 404(b) compliance imposes a significant burden on emerging biotech companies, citing the 2011 Staff Section 404(b) Study that estimated that companies with a public float between \$75 million and \$250 million spend, on average, \$840,276 to comply with Section 404(b).<sup>119</sup> Another commenter estimated that it will spend more than \$400,000 annually on compliance with Section 404(b).<sup>120</sup> One commenter that stated that its public float was more than \$75 million but less than \$250 million estimated that relief from Section 404(b) would result in a 35% reduction in compliance costs whereas there would be no material change in such costs from the proposed amendments.<sup>121</sup> Another commenter noted that, while most firms already take an integrated accounting approach to Section 404(b) requirements that

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<sup>115</sup> See Acorda, et al; AMTA; BIO; Calithera; Coalition; CONNECT; CSBA; and Seneca. See also Dixie.

<sup>116</sup> See Acorda, et al; BIO; CSBA; ICBA; and NVCA.

<sup>117</sup> See Acorda, et al; BIO; Calithera; CONNECT; CSBA (stating that “accelerated filers spend, on average, more than \$1 million complying with Section 404(b)”); Dixie; and Seneca.

<sup>118</sup> See Acorda, et al; and CONNECT. See also CSBA.

<sup>119</sup> See BIO.

<sup>120</sup> See Calithera. This estimate is generally consistent with the estimate set forth by a presenter at a recent ACSEC meeting. The presenter stated that some biotechnology companies that anticipate losing their status as EGCs in the next few years “believe they will incur somewhere between \$150,000 to \$350,000 in additional audit fees, \$50,000 to \$150,000 in other consulting costs and either \$40,000 or as much as \$200,000 for internal labor.” See Transcript of Presentation by William Newell at September 13, 2017 ACSEC Meeting available at <https://www.sec.gov/info/smallbus/acsec/acsec-transcript-091317.pdf> (pages 49 to 54); see also Newell, William J., “Sarbanes-Oxley Section 404(b): Costs of Compliance and Proposed Reforms”, presentation at ACSEC meeting on Sept. 13, 2017 available at <https://www.sec.gov/info/smallbus/acsec/william-newell-acsec-091317.pdf>.

<sup>121</sup> See Seneca.

includes a complete internal control review, if smaller companies were exempt from Section 404(b), they would avoid the added legal liability of the auditor attestation, providing a savings opportunity and lowering the cost of being public for those companies.<sup>122</sup>

A few commenters stated that the market does not value the audit of such internal control<sup>123</sup> or that the costs of Section 404(b) outweigh the benefits.<sup>124</sup> Another commenter stated that expanding relief from Section 404(b) to registrants with a public float of less than \$250 million would encourage capital formation because reduced audit and disclosure requirements may encourage companies that have been hesitant to go public to do so.<sup>125</sup>

A number of commenters recommended that the Commission allow a revenue test for the accelerated filer definition, similar to the amended revenue test being adopted by the Commission in the SRC definition.<sup>126</sup>

### **3. Final Amendments**

As proposed, we are adopting amendments to the “accelerated filer” and “large accelerated filer” definitions in Exchange Act Rule 12b-2 to preserve the application of the current thresholds contained in those definitions.<sup>127</sup> Specifically, we are eliminating from the definitions of accelerated filer and large accelerated filer the exclusions for registrants that are eligible to use the SRC requirements under Regulation S-K for their annual and quarterly reports.

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<sup>122</sup> See Dixie.

<sup>123</sup> See Acorda, et al (stating that the market does not demand a Section 404(b) audit as a prerequisite for investing in emerging, innovative companies and that virtually no EGCs are voluntarily forgoing their exemption from Section 404(b)). See also Dixie.

<sup>124</sup> See MidSouth.

<sup>125</sup> See ICBA (citing a 2005 ICBA study that estimated that audit fees for publicly held bank holding companies would drop dramatically – some by as much as 50% – if they were exempted from Section 404(b)).

<sup>126</sup> See Acorda, et al; AMTA; BIO; CONNECT; Calithera; CSBA; Nasdaq; and NYSE.

<sup>127</sup> See “accelerated filer” and “large accelerated filer” definitions in Exchange Act Rule 12b-2.

After the amendments to the SRC definition become effective, some SRCs will exceed the public float thresholds for initial or subsequent qualification in the accelerated filer definition, and a few of these registrants also may exceed the public float threshold for subsequent qualification in the large accelerated filer definition.<sup>128</sup>

Although we are not raising the accelerated filer public float threshold or modifying the Section 404(b) requirements for registrants with a public float between \$75 million and \$250 million in this release, as stated above, the Chairman has directed the staff to formulate recommendations to the Commission for possible changes to reduce the number of registrants that our rules define as accelerated filers. Eliminating the SRC provision in the accelerated filer and large accelerated filer definitions will maintain the current thresholds at which registrants are subject to the accelerated filer and large accelerated filer disclosure and filing requirements. In 2007, the Commission noted that aligning the SRC public float threshold based on the levels established for non-accelerated filers<sup>129</sup> was practical and avoided regulatory complexity.<sup>130</sup> These amendments will change the current relationship between the SRC and “accelerated filer” definitions by allowing a registrant to qualify as both a SRC and an accelerated filer.<sup>131</sup> We acknowledge the regulatory complexity created by this potential overlap between the SRC and

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<sup>128</sup> The only registrants that would qualify as both SRCs and large accelerated filers would be those companies (1) that previously qualified as large accelerated filers because at one time their public float was \$700 million or more, (2) whose revenues for the most recent fiscal year were less than \$100 million, and (3) whose public float as of the end of the most recent second quarter was less than \$560 million, such that they now qualify as SRCs, but not less than \$500 million, such that they are not eligible to exit large accelerated filer status.

<sup>129</sup> A non-accelerated filer is a filer that is not an “accelerated filer” or a “large accelerated filer.” See subpart (3) of the accelerated filer and large accelerated filer definitions in Exchange Act Rule 12b-2 [17 CFR 240.12b-2].

<sup>130</sup> See SRC Adopting Release 73 FR at 942.

<sup>131</sup> In conjunction with these amendments, we also are adopting technical revisions to Securities Act Forms S-1, S-3, S-4, S-8, and S-11 and Exchange Act Forms 10, 10-Q and 10-K. These amendments modify the cover page of the specified forms to remove the parenthetical next to the “non-accelerated filer” definition that states “(Do not check if a smaller reporting company).” After these amendments, a registrant should check all applicable boxes on the cover page addressing, among other things, non-accelerated, accelerated, and large accelerated filer status, SRC status, and emerging growth company status.

“accelerated filer” definitions.<sup>132</sup> As part of the staff’s consideration of possible recommended amendments to the “accelerated filer” definition, the Chairman has directed the staff to consider, among other things, the historical and current relationship between the SRC and “accelerated filer” definitions.

### **III. Other Matters**

If any of the provisions of these amendments, or the application thereof to any person or circumstance, is held to be invalid, such invalidity shall not affect other provisions or application of such provisions to other persons or circumstances that can be given effect without the invalid provision or application.

### **IV. Economic Analysis**

As discussed above, we are adopting amendments to the definition of SRC as used in our rules and regulations. The amendments expand the number of registrants that are eligible to provide scaled disclosure to their investors and are intended to reduce compliance costs for these registrants and promote capital formation, while maintaining appropriate investor protections. Registrants with a public float of less than \$250 million (an increase from the current \$75 million threshold) will qualify as SRCs, as will registrants with no public float if their revenues are less than \$100 million (an increase from the current \$50 million threshold).<sup>133</sup> In addition, registrants with a public float of less than \$700 million will qualify as SRCs if their revenues are less than \$100 million.<sup>134</sup>

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<sup>132</sup> Several commenters specifically recommended increasing the public float threshold in the accelerated filer definition to, among other things, maintain uniformity across our rules. *See* BIO; Coalition; Nasdaq; NVCA; and NYSE.

<sup>133</sup> *See* note 25 and related text for a discussion of how and when public float is calculated and when revenues are measured.

<sup>134</sup> The Commission received a number of comments in support of expanding the definition of SRC to include a revenue test for registrants with a public float. *See* Section II.A.1.b.



We also are making corresponding amendments to other rules in light of the new SRC definition. As proposed, we are adopting amendments to the “accelerated filer” and “large accelerated filer” definitions in Exchange Act Rule 12b-2 to preserve the application of the public float thresholds in those definitions. In addition, we are amending Rule 3-05(b)(2)(iv) of Regulation S-X to increase the revenue threshold under which certain registrants may omit the earliest of the three fiscal years of audited financial statements of an acquired business or business to be acquired.

We are mindful of the costs and benefits of the amendments. In this economic analysis, we examine the existing baseline, which consists of the current regulatory framework and market practices, and discuss the potential costs and benefits of the amendments, relative to this baseline, and their potential effects on efficiency, competition, and capital formation.<sup>135</sup> We also consider the potential costs and benefits of reasonable alternatives to the amendments. Where practicable, we have attempted to quantify the economic effects of the amendments; however, in certain cases, we are unable to do so because either the necessary data are unavailable or the economic effects are not quantifiable. In these cases, we provide a qualitative assessment of the likely economic effects.

#### **A. Baseline**

In calendar year 2016, 7,395 registrants filed a Form 10-K with the Commission. Excluding investment companies, business development companies, and ABS issuers, which are not eligible for SRC status, 6,739 registrants filed a Form 10-K in calendar year 2016. Of these

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<sup>135</sup> Section 23(a)(2) of the Exchange Act requires us, when adopting rules, to consider the impact that any new rule would have on competition. In addition, Section 2(b) of the Securities Act and Section 3(f) of the Exchange Act direct us, when engaging in rulemaking that requires us to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.

registrants, 2,592 (35.1% of all registrants) claimed SRC status by checking the box on the cover page of their Forms 10-K indicating that the registrant was a SRC. Under the current definition, a registrant with a public float may qualify as a SRC if its public float is less than \$75 million or a registrant with no public float may qualify as a SRC if its annual revenues are less than \$50 million. An additional 232 filers in calendar year 2016 reported public float of less than \$75 million or no public float and revenues of less than \$50 million, but did not check the box on the cover page of their Forms 10-K indicating that they were SRCs.<sup>136</sup> Of the 2,592 registrants that claimed SRC status in 2016, 1,899 registrants (25.7% of all registrants) reported having a public float that was less than \$75 million and 509 registrants (6.9% of all registrants) reported having no public float and revenues of less than \$50 million.<sup>137</sup> Of the 2,592 SRCs, 833 (11.3% of all registrants) also indicated in their filings that they were EGCs.<sup>138</sup>

Table 1 summarizes the number and percentage of registrants that claimed SRC status in each calendar year over the 2013-2016 period.

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<sup>136</sup> There are two potential explanations for why the number of registrants meeting the SRC thresholds exceeds the number of reported SRCs. First, the public float and revenue thresholds establish eligibility for SRC status, but do not require eligible registrants to take advantage of the scaled disclosure requirements. Thus, some registrants may be opting out of SRC status if they do not find the reduced compliance costs to be net beneficial. Second, some registrants that appear to be eligible may not be if they previously exceeded the SRC threshold and were required to meet the lower eligibility threshold (*i.e.*, public float of less than \$50 million or revenues of less than \$40 million) to subsequently qualify as a SRC.

<sup>137</sup> Based on analysis by DERA of available data. Staff obtained the SRC status and public float data from information extracted from exhibits to corporate financial reports filed with the Commission using eXtensible Business Reporting Language (“XBRL”), available at: <http://www.sec.gov/dera/data/financial-statement-data-sets.html>. Staff also extracted the SRC status and public float directly from Forms 10-K using a computer program. For robustness, staff compared the SRC status and public float information between the two sources and corrected discrepancies using data from Ives Group Audit Analytics. Staff extracted annual revenue data from the Compustat database and XBRL data in Form 10-K filings.

<sup>138</sup> Staff determined whether a registrant claimed EGC status by parsing several types of filings (for example, Forms S-1, S-1/A, 10-K, 10-Q, 8-K, 20-F/40-F, and 6-K) filed by that registrant with supplemental data drawn from Ives Group Audit Analytics.

**Table 1: SRCs in 2013-2016 Period**

Filing Year	Total # of Registrants	# of SRCs	% of Total	Qualified based on public float < \$75 million (% of Total)	Qualified based on no public float and revenue < \$50 million (% of Total)
2013	7,624	3,380	44.3%	33.5%	10.8%
2014	7,642	3,179	41.6%	32.7%	8.9%
2015	7,557	2,900	38.4%	29.7%	8.7%
2016	7,395	2,592	35.1%	25.7%	6.9%

Table 2 shows that, while registrants claiming SRC status with available data account for a substantial percentage of the total number of registrants in calendar year 2016, they account for less than one percent of the entire public float, market value and revenue of all registrants.<sup>139</sup>

**Table 2: Size Proxies for SRCs in 2016**

	Public Float	Market Value	Revenue
<b>Mean</b>	\$14.7 million	\$57.2 million	\$42.8 million
<b>Median</b>	\$4.3 million	\$14.1 million	\$1.9 million
<b>Aggregate size</b>	\$40.1 billion	\$98.7 billion	\$96.2 billion
<b>% of the aggregate size of all registrants</b>	0.15%	0.34%	0.66%

Table 3 shows the distribution of registrants that were eligible for SRC status based on available data in calendar year 2016 using the Fama-French 49-industry classification.<sup>140</sup> The “Business Services” industry accounts for 10.6% of all SRCs, followed by “Financial Trading”

<sup>139</sup> Compustat data on market value is obtained for calendar year 2016 filings. Staff obtained revenue data either from XBRL data in Form 10-K filings or directly from the filing itself. The summary statistics presented in Table 2 represent those registrants for which information on public float and revenue is concurrently available. Market value, as used throughout this Economic Analysis, is equivalent to market capitalization and presented for registrants with available data (described in footnote 25).

<sup>140</sup> The standard Fama-French classification sorts Standard Industry Classification codes into 49 main industrial categories; available at: [http://mba.tuck.dartmouth.edu/pages/faculty/ken.french/Data\\_Library/det\\_49\\_ind\\_port.html](http://mba.tuck.dartmouth.edu/pages/faculty/ken.french/Data_Library/det_49_ind_port.html).

(9.8%), “Pharmaceutical Products” (8.5%), “Banking” (7.1%), “Petroleum and Natural Gas” (5.6%), and “Computer Software” (5.2%).<sup>141</sup> We note that industries with a larger fixed component of operating costs, such as shipping, defense, and aircraft, tend to have fewer SRCs.

**Table 3: Industry Distribution of SRCs in 2016**

<b>Industry ID</b>	<b>Industry</b>	<b># of SRCs</b>	<b>% of all SRCs</b>	<b>Industry ID</b>	<b>Industry</b>	<b># of SRCs</b>	<b>% of all SRCs</b>
<b>1</b>	Agriculture	26	1.0%	<b>26</b>	Defense	2	0.1%
<b>2</b>	Food Products	35	1.3%	<b>27</b>	Precious Metals	38	1.4%
<b>3</b>	Candy & Soda	3	0.1%	<b>28</b>	Non-Metallic and Industrial Metal Mining	76	2.9%
<b>4</b>	Beer & Liquor	18	0.7%	<b>29</b>	Coal	3	0.1%
<b>5</b>	Tobacco Products	9	0.3%	<b>30</b>	Petroleum and Natural Gas	149	5.6%
<b>6</b>	Recreation	23	0.8%	<b>31</b>	Utilities	15	0.6%
<b>7</b>	Entertainment	55	2.0%	<b>32</b>	Communication	45	1.7%
<b>8</b>	Printing and Publishing	8	0.3%	<b>33</b>	Personal Services	37	1.4%
<b>9</b>	Consumer Goods	40	1.6%	<b>34</b>	Business Services	281	10.7%
<b>10</b>	Apparel	17	0.6%	<b>35</b>	Computers	22	0.8%
<b>11</b>	Healthcare	37	1.4%	<b>36</b>	Computer Software	136	5.2%
<b>12</b>	Medical Equipment	116	4.4%	<b>37</b>	Electronic Equipment	102	3.9%
<b>13</b>	Pharmaceutical Products	225	8.5%	<b>38</b>	Measuring and Control Equipment	41	1.6%
<b>14</b>	Chemicals	54	2.1%	<b>39</b>	Business Supplies	6	0.2%
<b>15</b>	Rubber and Plastic Products	20	0.8%	<b>40</b>	Shipping Containers	2	0.1%
<b>16</b>	Textiles	4	0.2%	<b>41</b>	Transportation	24	0.9%
<b>17</b>	Construction Materials	29	1.1%	<b>42</b>	Wholesale	78	3.0%

<sup>141</sup> In 2016, SRCs accounted for 57% of all Form 10-K filers in “Business Services,” 37% in “Financial Trading,” 20% in “Banking,” 39% in “Pharmaceutical Products,” 50% in “Petroleum and Natural Gas” and 47% in “Computer Software,” suggesting that these industries all have a fairly high concentration of small registrants.

**Table 3: Industry Distribution of SRCs in 2016**

<b>Industry ID</b>	<b>Industry</b>	<b># of SRCs</b>	<b>% of all SRCs</b>	<b>Industry ID</b>	<b>Industry</b>	<b># of SRCs</b>	<b>% of all SRCs</b>
<b>18</b>	Construction	22	0.8%	<b>43</b>	Retail	82	3.1%
<b>19</b>	Steel Works	9	0.3%	<b>44</b>	Restaurants, Hotels, Motels	28	1.1%
<b>20</b>	Fabricated Products	5	0.2%	<b>45</b>	Banking	187	7.1%
<b>21</b>	Machinery	54	2.0%	<b>46</b>	Insurance	20	0.8%
<b>22</b>	Electrical Equipment	39	1.5%	<b>47</b>	Real Estate	96	3.6%
<b>23</b>	Automobiles and Trucks	21	0.8%	<b>48</b>	Financial Trading	258	9.8%
<b>24</b>	Aircraft	8	0.3%		Other and Unknown	30	1.1%
<b>25</b>	Shipbuilding, Railroad Equipment	3	0.1%				

As discussed above, we are amending Rule 3-05(b)(2)(iv) of Regulation S-X to increase the revenue threshold under which certain registrants may omit the earliest of the three fiscal years of audited financial statements of an acquired business or business to be acquired. Rule 3-05 applies to registrants that are not SRCs.<sup>142</sup> Rule 3-05(b)(2)(iv) provides that, if the acquired business is large enough relative to the registrant (*i.e.*, any of the significant subsidiary tests for the acquired business exceed 50%), the registrant must file three years of historical financial statements of the acquired business unless the acquired business has revenues of less than \$50 million, in which case only two years of the acquired business's most recent financial statements need to be filed. Given the difficulty in accurately identifying registrants that have acquisitions (1) that meet any of the significant subsidiary tests at the 50% level and (2) where the acquired business has revenues of less than \$50 million, we are unable to estimate the number of

<sup>142</sup> Rule 8-04 of Regulation S-X [17 CFR 210.8-04] applies to financial statements of business acquired or to be acquired by SRCs.

registrants that were affected by the \$50 million revenue threshold in Rule 3-05(b)(2)(iv) in 2016. We do not believe the disclosure accommodation in Rule 3-05(b)(2)(iv) is frequently used because the acquired business not only would need to meet one of the significant subsidiary thresholds at the 50% level compared to the non-SRC acquirer, but also would need to have less than \$50 million of revenues in its most recent fiscal year.

## **B. Potential Economic Effects**

### **1. Introduction**

The primary benefit stemming from the amendments is a reduction in compliance costs for the registrants that will newly qualify for SRC status. To the extent that the reduced compliance costs have a fixed cost component,<sup>143</sup> which typically burdens smaller registrants disproportionately, the cost savings may be particularly helpful for those registrants.

As a secondary effect of the amendments, a lower disclosure burden could spur growth in the registrants that will newly qualify for SRC status to the extent that the compliance cost savings and other resources (*e.g.*, managerial effort) otherwise devoted to disclosure and compliance are productively deployed in alternative ways. It also could encourage capital formation because companies that may have been hesitant to go public may choose to do so if they face reduced disclosure requirements.

With respect to costs, we expect that the amendments to the SRC definition will result in a modest change in some indicators of the overall quality of the information environment.

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<sup>143</sup> See, *e.g.*, William A. Brock & David S. Evans, *The Economics of Small Businesses: Their Role and Regulation in the U.S. Economy* 65 at 70 (1986); C. Steven Bradford, *Does Size Matter? An Economic Analysis of Small Business Exemptions from Regulation*, College of Law, Faculty Publications. 72 (2004). See also Cindy R. Alexander et al., *Economic Effects of SOX Section 404 Compliance: A Corporate Insider Perspective*, 56 *J. Account. & Econ.* 267-290 at 285 (2013) (noting, among other things, that they found “evidence of fixed costs that weigh disproportionately on smaller firms”).

Generally, a decrease in the amount of direct disclosure could increase the information asymmetry between investors and company insiders, leading to lower liquidity and higher costs of capital for the affected registrants. For example, one study found that, during the three-month period following the establishment of the SRC definition, registrants with public floats of \$25 million or more and less than \$75 million that claimed SRC status experienced a significant reduction in liquidity relative to comparable registrants.<sup>144</sup> In addition, one of the sources of information asymmetry under the amendments will be that the newly eligible SRCs will not be required to provide certain executive compensation disclosures, potentially lowering corporate governance transparency of these registrants.<sup>145</sup> Furthermore, by introducing overlap between the SRC and the accelerated filer definitions, the amendments we are adopting would increase regulatory complexity.<sup>146</sup>

The number of affected registrants that will make scaled disclosures will ultimately depend on the choices of those registrants. That is, the SRC definition establishes eligibility for, but does not mandate reliance on, any of the scaled disclosure accommodations.<sup>147</sup> We identified 232 registrants in 2016 that met either the \$75 million public float threshold or the \$50 million revenue threshold for SRC status but did not claim SRC status. While some of these registrants may not have been eligible (for example, a registrant that previously did not qualify as a SRC

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<sup>144</sup> See Lin Cheng, Scott Liao, and Haiwen Zhang, *Commitment Effect versus Information Effect of Disclosure: Evidence from Smaller Reporting Companies*, 88 Account. Rev. 1239 (Jul. 2013).

<sup>145</sup> For a review of the effects of executive compensation disclosures on compensation practices, see Kevin J. Murphy, “Executive compensation: Where we are, and how we got there,” *Handbook of the Economics of Finance*, Vol. 2. Elsevier (2013) 211-356. See also Benjamin E. Hermalin and Michael S. Weisbach, *Information Disclosure and Corporate Governance*, 67 J. Fin. 195 (2012), and Anya Kleymenova and Irem A. Tuna, Regulation of Compensation (June 21, 2017), Chicago Booth Research Paper No. 16-07, available at SSRN: <https://ssrn.com/abstract=2755621>.

<sup>146</sup> See SRC Adopting Release 73 FR at 942.

<sup>147</sup> If a disclosure requirement applicable to SRCs is more stringent than for non-SRCs, however, SRCs must comply with the more stringent standard. Item 404 is the only Regulation S-K disclosure requirement that could be more stringent.

because it exceeded the thresholds and is now subject to a lower threshold), it is possible that some elected not to avail themselves of the scaled disclosure requirements.<sup>148</sup>

Under the amendments, we expect registrants will weigh their own costs and benefits of scaled disclosure and decide whether to take advantage of any of the scaled disclosure accommodations for which they are newly eligible. Some registrants may determine that the costs of potentially reduced liquidity for their securities and higher cost of capital exceed the benefits of the lower compliance costs. Those registrants may elect not to rely on the scaled disclosure accommodations available to them. On the other hand, expanding SRC eligibility could provide opportunities for adverse selection in a greater number of registrants. For example, registrants whose outside investors would have benefited from more disclosure might choose the less burdensome disclosure requirement once becoming eligible. The net benefit or cost for each newly eligible registrant and its investors will ultimately depend on the specific facts and circumstances.

Expanding the pool of registrants eligible for SRC status to include registrants with revenues of less than \$100 million and a public float of \$250 million or more and less than \$700 million will increase the cost savings, information asymmetries, and other effects of scaled disclosure in proportion to the increase in the number of registrants that become newly eligible at those higher thresholds and choose to avail themselves of the scaled disclosure accommodation. This number is likely to be small, as indicated by the evidence that 161 (2.2%) of the registrants that filed a Form 10-K in 2016 would have met the thresholds in the amended revenue test for

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<sup>148</sup> Data from 2008 show that registrants do not always take advantage of scaled disclosure. In a sample of 283 registrants that were newly eligible for scaled disclosure in 2008, the evidence from Form 10-K and proxy filings by those registrants shows that 109 of the registrants chose to maintain their disclosure level for all ten eligible items, while 174 of the registrants reduced the disclosure level for at least one eligible item. See Lin Cheng, Scott Liao, and Haiwen Zhang, *Commitment Effect versus Information Effect of Disclosure: Evidence from Smaller Reporting Companies*, 88 Account. Rev. 1239 (Jul. 2013) at 1247



registrants with public float.

The effects of scaled disclosure for registrants with a public float of \$250 million or more and less than \$700 million and revenues of less than \$100 million may be different from the effects of scaled disclosure for registrants with public float nearer to the current threshold of \$75 million. This is because the characteristics of registrants eligible for SRC status under the final rules may be different from those of registrants close to the current threshold. For example, differences in the relationships between management and outside investors in registrants with higher public float could affect the level of information asymmetries between those registrants and investors. This may cause those registrants to make different decisions about how much information they choose to disclose and whether to rely on the scaled disclosure accommodations, leading to differences in the observed use of scaled disclosure by different registrants of the same size. The 161 additional registrants had an average public float of \$396 million, while those that qualify under the current definition had an average public float of \$15 million, and those that would have qualified under the proposed rules had an average public float of \$55 million. These differences can affect whether a registrant decides to rely on scaled disclosure and how that decision affects the registrant's investors. We do not have sufficient information about the experiences of registrants at the higher public float levels with lower revenues implementing scaled disclosure to estimate the frequency with which these registrants will implement scaled disclosure, if available.

Similarly, increasing the revenue threshold below which registrants are eligible to provide two rather than three years of certain acquired businesses' historical financial statements under Rule 3-05(b)(2)(iv) from \$50 million to \$100 million will increase the cost savings, information asymmetries, and other effects of the reduced historical financial statement

disclosure that investors receive at or around the time of the acquisition in proportion to the increase in the number of registrants that acquire businesses with revenues below the higher threshold and choose to avail themselves of this disclosure accommodation.

Overall, we expect the effect of raising the revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X from \$50 million to \$100 million on information disclosed by registrants and its consequences for registrants and investors to be modest. This reflects our appraisal that few registrants are eligible to provide two rather than three years of an acquired business's historical financial statements under Rule 3-05(b)(2)(iv), because the acquired business not only would need to meet one of the significant subsidiary thresholds at the 50% level compared to the non-SRC acquirer, but the acquired business also would need to have less than the \$50 million of revenues in its most recent fiscal year.<sup>149</sup> The amendments we are adopting will have two potentially countervailing effects on the number of registrants that are eligible for the disclosure accommodation in Rule 3-05(b)(2)(iv). First, they will increase the number of registrants that are eligible to provide two rather than three years of an acquired business's historical financial statements under Rule 3-05(b)(2)(iv) by raising the revenue threshold for eligibility. Second, they will reduce the number of registrants that are required to comply with Rule 3-05, because Rule 3-05 is only applicable to registrants that are not SRCs, and our final rules are likely to increase the number of SRCs. Thus, the net effect may be to increase the number of registrants eligible to provide two rather than three years of an acquired business's historical financial statements under Rule 3-05(b)(2)(iv), but we do not expect the net increase to be significant.

## **2. Impact on Eligibility for Smaller Reporting Company Status**

By increasing the public float threshold from \$75 million to \$250 million, increasing the

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<sup>149</sup> See text accompanying note 142.

annual revenue threshold for registrants with no public float from \$50 million to \$100 million, and expanding the revenue test to include registrants with a public float of less than \$700 million and revenues of less than \$100 million in the SRC definition, the amendments will permit more registrants to qualify as SRCs. To estimate the number of additional registrants that are likely to be affected by the amendments, we use public float data and revenue data from Form 10-K filings.<sup>150</sup> Our estimate of the number of registrants likely to be eligible in the first year under the new definition that would not have qualified under the current definition is the number that would have been eligible had the rule been in effect. We use evidence on the composition of those registrants from the 2016 data to estimate the likely composition of the registrants that would be eligible in the first year under the new definition.

We estimate that 966 additional registrants will be eligible for SRC status in the first year under the new definition. These registrants estimated to be eligible in the first year comprise 779 registrants with a public float of \$75 million or more and less than \$250 million, 26 registrants with no public float and revenues of \$50 million or more and less than \$100 million, and 161 registrants with a public float of \$250 million or more and less than \$700 million and revenues of less than \$100 million.

The 966 registrants that we estimate will be newly eligible for SRC status are characterized by an average public float of \$191 million (median \$162 million), an average market value of \$279 million (median \$201 million), and average revenues of \$196 million (median \$68 million). Of these registrants, 365 currently are EGCs and are eligible for certain scaled disclosure under Title I of the JOBS Act, including the scaled executive compensation

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<sup>150</sup> Float and revenue values are from data in Form 10-K filings filed in calendar year 2016 and extracted from XBRL exhibits.

disclosures available to SRCs under Item 402 of Regulation S-K. The newly eligible registrants with available data in 2016 were concentrated in the following industries: “Pharmaceutical Products” (17.3%), “Banking” (15.2%), “Financial Trading” (11.8%), “Business Services” (5.2%), and “Electronic Equipment” (3.7%). If the distribution of eligible registrants does not change over time, and if all of them claim SRC status, the amendments will lead to a noticeable increase in the presence of “Pharmaceutical Products” and “Banking” registrants in the pool of SRCs.

Registrants eligible for SRC status with available data using the public float threshold of less than \$250 million represent approximately 38.6% of all registrants, while only 28.0% of all registrants qualify under the existing public float threshold of less than \$75 million. The 38.6% of all registrants that will qualify under the public float threshold would be more in line with the 42% of registrants that qualified under the public float threshold when the Commission first established the definition of SRC.<sup>151</sup> An additional 8.0% of registrants will qualify based on having no public float and revenues of less than \$100 million, while currently 7.7% of registrants reported having no public float and less than \$50 million in revenues.<sup>152</sup> Finally, based on the 2016 data, 2.2% of registrants had a public float of \$250 million or more and less than \$700 million and revenues of less than \$100 million.

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<sup>151</sup> These percentages reflect the estimated number of registrants that qualify under the respective public float tests and do not include any registrants that are estimated to qualify under the respective revenue tests.

<sup>152</sup> Using 2016 data, we estimate that, of the 7,395 total registrants that filed Forms 10-K with available data, 3,606 registrants will meet one of the SRC thresholds under the amendments. In particular, we estimate that 2,851 registrants reported public float below \$250 million and greater than zero in 2016, resulting in a percentage of 38.6% (2,851/7,395) of registrants potentially qualifying as SRCs under the amended public float threshold, and 2,072 registrants reported a public float below \$75 million in 2016, resulting in a percentage of 28.0% (2,072/7,395). Also, we estimate that 594 registrants reported no public float and annual revenues below \$100 million in 2016, resulting in a percentage of 8.0% (594/7,395) of registrants potentially qualifying as SRCs under the amended revenue threshold, and 568 registrants reported no public float and annual revenues below \$50 million in 2016, resulting in a percentage of 7.7% (568/7,395). Finally, we estimate that 161 registrants reported public float of \$250 million or more and less than \$700 million and annual revenues below \$100 million in 2016, resulting in an additional 2.2% (161/7,395) of registrants potentially qualifying as SRCs.

Increasing the percentage of registrants that will qualify under the public float threshold to align more closely with the 2007 level is consistent with the rise in market capitalization of public companies that has occurred since that time.<sup>153</sup> We do not have sufficient data to be able to compare the percentage of registrants qualifying under the revenue threshold when the Commission first established the definition of SRC to the estimated 8.0% that will qualify using a revenue threshold of \$100 million. Table 4 summarizes the size of the potential SRCs in terms of public float, market value, and annual revenue under the amendments.

**Table 4: Size Proxies for SRCs Eligible Under the Amendments**

	<b>Public Float</b>	<b>Market Value</b>	<b>Revenue</b>
<b>Mean</b>	\$59.9 million	\$480.1 million	\$317.7 million
<b>Median</b>	\$12.1 million	\$40.9 million	\$10.3 million
<b>Aggregate size</b>	\$202.6 billion	\$1,220.5 billion	\$1,074.0 billion
<b>% of the aggregate size of all registrants</b>	0.9%	4.8%	8.7%

As discussed above, we are amending Rule 3-05(b)(2)(iv) of Regulation S-X to increase the revenue threshold under which certain registrants may omit the earliest of the three fiscal years of audited financial statements of an acquired business or business to be acquired. Similar to the baseline discussion of Rule 3-05, given the difficulty in accurately identifying registrants that have acquisitions (1) that meet any of the significant subsidiary tests at the 50% level and (2) where the acquired business has revenues of less than \$100 million, we are unable to estimate the number of registrants that will be affected by raising the revenue threshold in Rule 3-05(b)(2)(iv) from \$50 million to \$100 million. The amendments we are adopting today increase the number of registrants that qualify as SRCs (which will likely decrease the application of Rule 3-05) but

<sup>153</sup> For example, the S&P 500 index grew by more than 80 percent over the decade ending with the fourth quarter of 2017. Source: CRSP and St. Louis Fed (<https://fred.stlouisfed.org/series/GDPDEF>).

also increase the revenue threshold in Rule 3-05(b)(2)(iv) (which may offset the decreased number of companies affected by Rule 3-05). Therefore, we do not expect that the amendments will significantly alter the number of registrants that will be eligible to omit the earliest of three years of financial statements of an acquired business pursuant to Rule 3-05(b)(2)(iv).

### **3. Estimation of Potential Costs and Benefits**

In this section, we estimate the incremental costs and benefits associated with SRC-related scaled disclosures, using a multivariate empirical analysis. We cannot isolate the costs and benefits associated with scaled disclosures using available data from SRCs, because we cannot with the data isolate the effects of scaled disclosures from the effects of some other accommodations, such as the exemption from Section 404(b) that is currently available to all SRCs through their status as non-accelerated filers.<sup>154</sup> Under the final rules, some newly eligible SRCs will be able to provide scaled disclosures but will continue to be subject to Section 404(b) as accelerated filers.

It is possible, however, to isolate the effects of scaled disclosures on registrants with public float slightly below or above the current \$75 million public float threshold using 2006-2009 data. This is because, as a result of the rules that established the SRC definition in 2007, registrants with public float of \$25 million or more and less than \$75 million experienced no change in the Section 404(b) exemption (that is, they remained exempt from the requirement), but became eligible for the SRC scaled disclosures. Our empirical method is a difference-in-

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<sup>154</sup> Although there is a clear threshold for eligibility, we cannot use the well-known empirical method of Regression Discontinuity Design to assess the treatment effect of scaled disclosures for SRCs. This method requires that the assignment of the treatment among registrants be “as good as random” around the threshold. Under this assumption, the registrants that receive the treatment of scaled disclosure (*i.e.*, SRCs) should be comparable to those registrants that do not receive the treatment because their public float is just above the \$75 million threshold. Given the exemption from Section 404(b) available to current SRCs with public float below \$75 million, this assumption does not hold.

difference estimation between a treatment group and a control group that is the basis for comparison.<sup>155</sup> In particular, the treatment group (“Treatment Group”) consists of registrants with public float of \$25 million or more and less than \$75 million that claimed SRC status in 2008. Two natural control groups exist. The first (“Control Group 1”) consists of registrants that did not qualify for SRC status because they had public float at or just above \$75 million (\$75 million or more and less than \$125 million).<sup>156</sup> The second (“Control Group 2”) consists of registrants with public float and revenues below \$25 million that were already eligible for scaled disclosures at that time and thus not affected by the Commission’s 2007 rules.<sup>157</sup>

To analyze the economic effects of eligibility for scaled disclosures resulting from the Commission’s 2007 rules by this method, we compare the Treatment Group with Control Group 1 and Control Group 2 in the following areas: cost savings, information environment, liquidity, and growth. We then use the analysis to extrapolate the likely effects of the expansion of eligibility for SRC status under the final rules. In extrapolating the likely effects, we place particular emphasis on the comparison between the Treatment Group and Control Group 1, which represents a closer group in size to the newly eligible SRCs under the final rules.

We believe that the evidence from analysis of changes in the information environments of registrants around the 2007 amendments is a suitable basis for evaluating the effects of the

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<sup>155</sup> Difference-in-difference is a technique used to calculate the effect of a variable on a treatment group versus a control group. In particular, in the analysis below, the average change over time in the outcome of a variable for the treatment group is compared to the average change over time in the outcome of that variable for the control group.

<sup>156</sup> This would allow for a \$50 million bandwidth similar to that used in the Commission’s 2007 rules, which raised the threshold for relief from \$25 million to \$75 million.

<sup>157</sup> The comparison groups help control for confounding factors that may also independently affect the economic effects associated with scaled disclosures. While we determine Treatment Group and Control Group 1 based on public float alone, we use both public float and revenues to determine Control Group 2, because, prior to the Commission’s 2007 rules, registrants with public float below \$25 million were not eligible for scaled disclosures if their revenues exceeded \$25 million.

current amendments on registrants with public floats at the low end of the range that are newly eligible for scaled disclosure. We included a similar analysis in the Proposing Release and solicited comments on this analysis, including ways to better quantify the effects of scaled disclosure on SRCs, but did not receive any comments in response.

While the 2007 amendments resulted in changes that are similar to what we expect will occur under the current amendments, our analysis is subject to a number of assumptions and limitations. The evidence from the 2007 amendments may be less suitable as a basis for evaluating the effects of the current amendments on registrants with relatively higher levels of public float than for evaluating potential effects of the current amendments on registrants with public float around the \$75 million threshold.<sup>158</sup> It is thus more challenging to quantify the likely effects of the current amendments on newly eligible SRCs with public float levels that are farther from the \$75 million level, such as those closer to the \$250 million and \$700 million levels.<sup>159</sup> We believe those challenges may be less pronounced for registrants that have other characteristics, such as revenue, similar to those of the registrants that were affected by the prior rules.

**a. Potential Cost Savings: Estimates Based on Changes in Audit Fees**

The cost savings from scaled disclosures could include savings of resources that are likely to be used for the relevant parts of disclosures, for example, managerial and employee time, other internal resources, and audit fees related to certain disclosures. Among these

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<sup>158</sup> The 2007 rule amendments affected the reporting practices of registrants with public floats near the \$75 million threshold (*i.e.*, \$25 million or more and less than \$75 million) and, accordingly, may indicate the effects of increasing the public float threshold on registrants with public float of \$75 million or slightly more than \$75 million.

<sup>159</sup> One limitation of difference-in-difference and regression discontinuity design studies of the effects of changes in regulatory rules is that their results are more applicable in evaluating the effects of the changes on the registrants whose characteristics most closely resemble those who were affected by the event under the analysis than in evaluating effects on other registrants. *See, e.g.*, Leuz and Wysocki (2016).



potential savings, changes in audit fees are readily quantifiable. To the extent that the scaled disclosure accommodations affect information that must be audited, scaled disclosures of the audited portions of the filings should lead to a reduction in audit expenses. Because many of the scaled disclosures available to SRCs relate to governance and executive compensation disclosures that are not subject to audit, a reduction in audit fees is likely a small part of the total cost savings associated with scaled disclosures. However, quantifying the change in audit fees can potentially help us estimate the entire cost savings.

To estimate the cost savings from the amendments, we first examine changes in the audit fees of registrants that were newly eligible to use scaled disclosures as a result of the 2007 amendments relative to those in the control, or comparison, groups between the pre-amendment 2006-2007 period and the post-amendment 2008-2009 period. Audit fee data come from the Ives Group Audit Analytics database. We include only registrants that had both pre-amendment and post-amendment audit fee data in the analysis. Table 5 reflects the general results.

**Table 5: Pre- and Post-Commission’s 2007 Amendments Audit Fees for SRCs and Control Groups**

Fiscal Year	Treatment Group (SRCs w/ public float \$25m- \$75m)	Control Group 1 (Non-SRCs w/ public float \$75m- \$125m)	Control Group 2 (SRCs w/ public float and revenues below \$25m)
Avg. 2006-2007	\$311,105	\$676,194	\$113,757
Avg. 2008-2009	\$267,252	\$654,463	\$101,854
Number of Observations	1,315	694	962

For SRCs with public floats of \$25 million or more and less than \$75 million, in 2008-2009, average audit fees declined by \$43,853. In contrast, both Control Group 1, which just missed eligibility for SRC status, and Control Group 2, which already was eligible for scaled disclosures, experienced smaller declines in average audit fees after the adoption of the 2007 amendments: \$21,731 and \$11,903, respectively. Thus, the difference-in-difference estimate of

the savings in audit fees associated with scaled disclosures is between \$22,122 and \$31,950 per SRC with public float around the \$75 million threshold. Although two different control groups are used to control for other factors that may have caused the changes in audit fees noted in Table 5 during the 2006-2009 period,<sup>160</sup> the effect of the 2008 financial crisis may not be completely ruled out and could make the estimated savings in audit fees appear larger than they actually were.

We also estimate the savings in audit fees in terms of a percentage reduction, instead of a dollar value.<sup>161</sup> The audit fees for the Treatment Group declined by 14.1% in the 2008-2009 period relative to the 2006-2007 period, but only by 3.2% for Control Group 1 and 10.5% for Control Group 2. Thus, the difference-in-difference estimate of the treatment effect in terms of a percentage reduction is a 3.6% to 10.9% reduction in the audit fees.

For the 966 newly eligible registrants that we estimate would be potentially affected by the amendments, the average audit fees were \$658,735 in fiscal year 2016. Thus, if we use the dollar value estimates of the audit fee savings, the estimated reduction in audit fees would be between \$28,490 and \$41,147 for this group, which are the inflation-adjusted values of the audit

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<sup>160</sup> For example, among other factors, we note that the Commission approved Public Company Accounting Oversight Board Auditing Standard No. 5 regarding Audits of Internal Control over Financial Reporting (AS 5). Among other things, AS 5 was intended to reduce unnecessary costs by making the audit scalable to fit the size and complexity of a company. AS 5 became effective in November 2007, and registrants with fiscal years ending between July and November were allowed to avail themselves of the provision earlier. The adoption and implementation of AS 5 in 2007 could have had an impact on the audit fees of all registrants subject to Section 404(b). Given that in our analysis both Treatment Group and Control Group 1 were affected by AS 5, however, the difference-in-difference methodology should control for the potential effects of AS 5 on audit fees. In addition, based on registrants' fiscal year end, we have no reason to believe that early adopters were more or less concentrated in Treatment Group than Control Group 1. *See also* Commission Guidance Regarding Management's Report on Internal Control Over Financial Reporting Under Section 13(a) or 15(d) of the Securities Exchange Act of 1934, Release No. 33-8810 (Jun. 20, 2007) [72 FR 35324 (Jun. 27, 2007)].

<sup>161</sup> If there is a fixed (dollar value) component in audit expenses that apply to registrants of all sizes, then the estimates under this alternative approach can be viewed as the upper bound of the potential audit fee savings.

fee savings estimates in 2008 and 2009.<sup>162</sup> This estimate of savings on audit fees for the newly eligible registrants is approximately 4.3% (\$28,491/\$658,735) to 6.2% (\$41,148/\$658,735) of the audit fees.

We recognize that this analysis of the audit fee data is subject to a number of assumptions, some of which may not be fully applicable when estimating the potential change in audit expenses as a result of the amendments.<sup>163</sup> As a result, there are limitations to our ability to draw conclusions from the analysis. For example, we recognize that audit expenses are only one component of costs for registrants and that changes in audit fees do not capture the full range of potential cost savings stemming from scaled disclosures. There are cost savings apart from the audit, such as cost savings resulting from a SRC not being required to prepare a compensation discussion and analysis and from other scaled disclosures in Item 402 of Regulation S-K. These cost savings likely will include both internal cost savings (such as employee and managerial time and resources) and external cost savings from fees for other outside professionals such as attorneys. Given the nature of scaled disclosures available to SRCs, we expect these other cost savings to be much larger than the cost savings in audit fees. In the Proposing Release, we assumed that 25% of the total cost savings from scaled disclosure comes from savings in audit fees and 75% of the savings comes from reduction in other expenses. We solicited comments on this assumption and on whether we should use a different assumption but did not receive any

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<sup>162</sup> The inflation adjustment was performed using the CPI calculator of the Bureau of Labor Statistics (<http://data.bls.gov/cgi-bin/cpicalc.pl>).

<sup>163</sup> Estimates based on data from 2006 to 2009 may not be directly applicable to the estimation of audit fees for the newly eligible registrants under the rule amendments. On the one hand, because auditors may charge larger registrants more for auditing the same disclosure items, our estimate could be viewed as a conservative estimate on the potential savings of audit fees for the newly eligible SRCs. On the other hand, if there were any increased competition in the auditing industry since 2009, then it could have led to lower audit expenses for the same disclosure items. Thus, our estimate could be higher or lower than the actual savings on audit fees for SRCs in 2008 and 2009.

comments in response. Accordingly, we use the same assumption here.

Given this assumption, we estimate total annual cost savings per newly eligible registrant with a public float around the \$75 million threshold to be between \$98,439 ( $\$24,610 \times 4$ ) and \$298,052 ( $\$74,513 \times 4$ ). The savings to registrants that become newly eligible with public floats closer to the \$250 million and \$700 million thresholds, will vary from this estimate by amounts that are difficult to quantify, because these registrants are less comparable to the Control Groups, and will depend on the facts and circumstances of the newly eligible registrant. For example, the audit cost for some of these registrants may be higher as a result of greater complexity in their business operations, increasing the cost savings associated with SRC status.

**b. Information Environment, Liquidity, and Growth**

A registrant's information environment can be measured by the amount of useful information available to investors and the quality of that information. To gauge the potential effects on the degree of external information production about the registrant that could benefit investors, we determine a registrant's percentage of institutional ownership, total 5% block institutional ownership, and analyst coverage (*i.e.*, whether a registrant is covered by at least one analyst and the number of analysts).

To measure disclosure quality, we use four discretionary accrual measures commonly used in the accounting literature as proxies for earnings management and the incidence of material restatements (based on the first year of financial statements restated and the filing year). Scaled disclosure may contribute to lowering the overall quality of the information environment, which is proxied in this analysis by the propensity for earnings management and the incidence of

material restatements.<sup>164</sup> The data on restatements are from the Ives Group Audit Analytics database. A material restatement is defined as a restatement that is reported under Item 4.02 of Form 8-K.

To examine the potential effects on liquidity, we focus on the share turnover ratio, which is calculated by dividing the total number of shares traded over a period by the number of shares outstanding. To assess the effects of scaled disclosures on growth, we examine a registrant's capital investment, which is measured by the capital expenditures to assets ratio, as a proxy for real growth. Because there is a high concentration of SRCs in industries for which research and development ("R&D") investment is important (*e.g.*, pharmaceutical products and electronic equipment), we also examine a registrant's investment in R&D. Finally, we examine asset growth, which is the growth rate in book assets, which could capture a registrant's growth through both capital investment and acquisition.

Table 6 reports the estimated treatment effect. The number in the Treatment Group vs. Control Group 1 column reflects the difference between: (1) the average change in the metric for the Treatment Group, from the 2006-2007 period, when it was not eligible for scaled disclosure, to the 2008-2009 period, when it was eligible for scaled disclosure, and (2) the average change in the metric between the same periods for Control Group 1, which was never eligible for scaled disclosure. Similarly, the number in the Treatment Group vs. Control Group 2 column reflects the difference between: (1) the average change in the metric for the Treatment Group from the 2006-2007 period, when it was not eligible for scaled disclosure, to the 2008-2009 period, when it was eligible for scaled disclosure and (2) the average change in the metric between the same

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<sup>164</sup> In using these proxies, we do not mean to suggest that scaled disclosure would be expected to directly cause an increase in earnings management or an increased incidence of material restatements, as there is little direct connection between the types of disclosure governed by our scaled disclosure requirements and the disclosure affected by a restatement.

periods for Control Group 2, which had been eligible for scaled disclosure for both periods.<sup>165</sup>

**Table 6: Scaled Disclosures and the Information Environment, Liquidity, and Growth<sup>166</sup>**

	Treatment Group vs. Control Group 1	Treatment Group vs. Control Group 2
Information Environment:		
External Information Production		
Institutional Ownership	-0.052***	-0.022***
Institutional Block Ownership	-0.016**	-0.002
Number of Analysts	-0.179	-0.068
Analyst Coverage Dummy	-0.099***	0.087***
Information Environment:		
Disclosure Quality		
Earnings Mgmt. 1	0.025	0.015
Earnings Mgmt. 2	0.024	0.013
Earnings Mgmt. 3	0.020	0.024
Earnings Mgmt. 4	0.018	0.023
Material Restatement (Filing Year)	0.018	0.015
Material Restatement (First Year Restated)	0.036**	0.016

<sup>165</sup> Specifically, for each number reported in Table 6, we estimate the following equation:

$$y = a + b * SRC + c * After + d * [SRC * After]$$

where the single-letter terms “a” to “d” are coefficients to be estimated; “SRC” equals one for the treatment group and zero for the comparison group; and “After” equals one for fiscal years 2008 and 2009 and zero for fiscal years 2006 and 2007. The treatment effect is reflected in the coefficient estimate *d*, which is the differential value of the variable *y* for treated firms following the start of the treatment. A statistically negative estimate of *d* is consistent with a reduction in the value of the dependent variable *y* (Institutional Ownership, Institutional Block Ownership, etc.) for treated firms.

<sup>166</sup> This table shows changes in the information environment, liquidity, and growth upon the introduction of scaled disclosure for SRCs. Treatment Group consists of SRCs with public float of \$25 million or more and less than \$75 million in fiscal year 2008. Control Group 1 consists of non-SRCs with public float of \$75 million or more and less than \$125 million. Control Group 2 consists of small business issuers with public float and revenues below \$25 million. Institutional Ownership is total percentage institutional ownership. Block Institutional Ownership is total block (5%) institutional ownership. Number of Analysts is the number of analysts following a registrant. Analyst Coverage Dummy is a dummy variable indicating the existence of analyst following. Earnings Mgmt. 1-4 are four different discretionary accruals measures. Earnings Mgmt. 1 follows Kothari, Leone, and Wasley (2005), and Earnings Mgmt. 2-4 follows Dechow, Sloan, and Sweeney (1995).<sup>166</sup> Material Restatement (Filing Year) is a dummy variable that equals one if a registrant discloses restatement under Item 4.02 of Form 8-K in that year, and zero otherwise. Material Restatement (First Year Restated) is a dummy variable that equals one if the material reason for the restatement under Item 4.02 of Form 8-K originated in that year, and zero otherwise. Share Turnover is the ratio of shares traded over shares outstanding. Capital Investment is capital expenditures over book assets. R&D investment is R&D expenditures over revenue. Asset Growth is the annual growth rate of book assets. \*\*\*, \*\*, and \* indicate significance at 1%, 5%, and 10% confidence levels, respectively.

	Treatment Group vs. Control Group 1	Treatment Group vs. Control Group 2
Liquidity		
Share Turnover Ratio	-0.063	-0.052
Growth		
Capital Investment	0.005	-0.005
R&D Investment	-0.035	-0.002
Asset Growth Rate	-0.005	-0.282***

The results in Table 6 suggest that the scaled disclosures had a negative effect on institutional ownership. The Treatment Group, which became eligible for scaled disclosures, experienced a 5.2% greater decrease in average institutional ownership from period to period than the registrants in Control Group 1, which remained ineligible for scaled disclosures, and a 2.2% greater decrease in average institutional ownership from period to period than the registrants in Control Group 2, which were eligible for scaled disclosures throughout both periods.

The results reflect a positive effect on material restatements in SRCs based on the first year restated, while the effect on analyst coverage is inconclusive. SRCs tend to lose analyst coverage relative to comparable registrants that just missed eligibility, but they gain coverage relative to even smaller registrants that already were eligible for scaled disclosures. There is no statistically significant effect on earnings quality as captured by discretionary accruals measures or the incidence of material restatement based on when the restatement was filed. Overall, the evidence suggests a modest, but statistically significant, negative effect of scaled disclosure on SRCs' overall information environment.

The effect of scaled disclosures on share turnover ratio is negative but statistically

insignificant, suggesting no significant effect of scaled disclosures on SRCs' liquidity.<sup>167</sup>

Because the newly eligible registrants are larger in market value and have more institutional ownership and analyst coverage than the current SRCs, to the extent those registrants rely on the accommodations, we do not expect a significant negative impact on their liquidity.

The results in Table 6 indicate no clear difference between SRCs and registrants in Control Group 1 and Control Group 2 in terms of changes in capital investment and R&D investment. The effect on asset growth rate is mixed. There is no significant difference between the Treatment Group and Control Group 1, but compared to Control Group 2, the Treatment Group had deterioration in asset growth rate after the 2007 rules. Overall, our empirical analysis suggests that scaled disclosures have only a minimal effect on growth in current SRCs relative to the Control Groups. Thus, we do not expect the use of scaled disclosures to have a significant effect on the growth of the newly eligible registrants under the final rules.

**c. Rule 3-05**

Similar to our discussion of the amendments to the SRC definition, we generally expect a modest reduction in compliance costs for registrants that are eligible to provide two rather than three years of historical financial statements of certain acquired businesses under Rule 3-05(b)(2)(iv), with corresponding potential modest increases in information asymmetries. We expect the magnitude of the effects of the change in the revenue threshold in Rule 3-05(b)(2)(iv) to be smaller for those registrants that acquire relevant businesses and their investors, as

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<sup>167</sup> In contrast, Chang et al. (2013) did find a negative and significant effect of the Commission's 2007 amendments on SRCs' liquidity. The difference in the results could stem from the use of a different empirical methodology, sample, and sample period. Chang et al. (2013) excluded financial companies. While the authors examined a pre-amendment period of April to June 2007, we included the entire 2006 and 2007 periods. Also, while the authors examined a post-amendment period of February to August 2008, we included the entire 2008 and 2009 periods. In addition, the authors focus on a set of illiquidity measures, while we focus on the share turnover ratio, a commonly used liquidity measure.



compared to the change in the SRC definition for newly eligible registrants and their investors. The reason for this expectation is that the revenue threshold in Rule 3-05(b)(2)(iv) only affects the historical financial statements of the acquired businesses (by limiting them to two years rather than three years), whereas a registrant that qualifies as a SRC will be able to comply with a number of scaled disclosure accommodations, including providing two years of financial statements and scaled executive compensation disclosures.<sup>168</sup>

#### **d. Conclusion**

Taken together, our empirical analysis suggests that, for most of the newly eligible SRCs under the final rules, scaled disclosures may generate a modest, but statistically significant, amount of cost savings in terms of the reduction in compliance costs, a modest, but statistically significant, deterioration in some of the proxies used to assess the overall quality of information environment, and a muted effect on the growth of the registrant's capital investments, investments in R&D, and assets. We expect the effects on registrants that are newly eligible for reduced disclosure under Rule 3-05(b)(2)(iv) to be lesser in magnitude but qualitatively similar.

#### **4. Affiliated Ownership and Adverse Selection**

In general, holding market value constant, the use of public float to define eligibility favors registrants with more affiliated ownership. If we consider two registrants with the same market value but different affiliated ownership, the one with greater affiliated ownership will have a lower public float, which is the value of non-affiliated ownership, and thus will be more likely to qualify for SRC status based on the public float threshold. This could be problematic if the adverse selection problem creates a conflict of interest between affiliated owners—who are often the decision makers—and non-affiliated owners—who are often the uninformed minority

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<sup>168</sup> See Section I for a discussion of the scaled disclosure accommodations available to SRCs.

shareholders on whom reduced disclosure may have a greater impact. We examine whether the effects of scaled disclosure on registrants' information environment, liquidity, and growth depend on the percentage of affiliated ownership, which is the market value of affiliated equity shares divided by the registrant's total market value of equity. The average affiliated ownership is 43% for SRCs in the treatment group in years 2008 and 2009 (median 42%). Specifically, we examine whether and to what extent the effects of scaled disclosure on information environment, liquidity, and growth differ for SRCs with high, or above-average, affiliated ownership as compared to low, or below-average, affiliated ownership.

The results are reflected in Table 7. The number in the Treatment Group vs. Control Group 1 column reflects the difference between: (1) the difference between the average metric of registrants in the Treatment Group with affiliated ownership that is higher than the group median and that of the registrants in the Treatment Group with affiliated ownership that is lower than the group median and (2) the difference between the average metric of registrants in Control Group 1 with affiliated ownership that is higher than the group median and that of the registrants in Control Group 1 with affiliated ownership that is lower than the group median. Similarly, the number in the Treatment Group vs. Control Group 2 column reflects the difference between: (1) the difference between the average metric for the higher-than-median affiliated ownership registrants and that of the lower-than-median affiliated ownership registrants in the Treatment Group and (2) the difference between the average metrics for the same sectors of Control Group 2.<sup>169</sup>

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<sup>169</sup> Specifically, for each number reported in Table 7, we estimate the following equation:

$$y = a + b * SRC + c * After + d * HighAff + e * [SRC * After] + f * [SRC * HighAff] + g * [After * HighAff] + h * [SRC * HighAff * After]$$

**Table 7: Affiliated Ownership and Adverse Selection**<sup>170</sup>

	Treatment Group vs. Control Group 1	Treatment Group vs. Control Group 2
Information Environment:		
External Information Production		
Institutional Ownership	-0.127***	-0.110*
Institutional Block Ownership	-0.079**	-0.126*
Number of Analysts	-0.742**	1.277**
Analyst Coverage Dummy	-0.052	0.500**
Information Environment:		
Disclosure Quality		
Earnings Mgmt. 1	0.010	0.286
Material Restatement (Filing Year)	0.038	-0.040
Material Restatement (Beginning Year)	0.084**	0.001
Liquidity		
Share Turnover Ratio	0.052	0.059
Growth		
Capital Investment	0.029**	0.049
R&D Investment	0.014	-0.756
Asset Growth Rate	0.136	-1.485

Our analysis suggests that affiliated ownership may exacerbate the potential negative effects of scaled disclosure on external information production by professionals such as institutional investors. There is also some evidence that larger affiliated ownership may exacerbate the adverse effect of scaled disclosure on material restatements based on when such restatement was triggered in SRCs (relative to Control Group 1). At the same time, scaled

where the single-letter terms “a” to “h” are coefficients to be estimated. “After” and “SRC” are defined in note 165. “HighAff” is a dummy variable equal to one if the firm’s affiliated ownership is greater than the sample median of 0.42; otherwise, “HighAff” is equal to zero. The treatment effect of interest is measured by the coefficient *h*, which is the differential value of the variable *y* for treated firms with high affiliated ownership, following the start of the treatment. *See also* note 165.

<sup>170</sup> This table shows the differences in the changes between registrants with high affiliated ownership and those with low affiliated ownership upon the introduction of scaled disclosure for SRCs. Affiliated ownership is the percentage of a registrant’s market value of equity that is owned by affiliated parties (*i.e.*, corporate insiders and 10% block owners). Registrants with high (low) affiliated ownership include registrants with affiliated ownership above (below) the sample median. A negative and significant estimate means that scaled disclosures have a more negative effect on SRCs with high affiliated ownership than on those with low affiliated ownership. \*\*\*, \*\*, and \* indicate significance at 1%, 5%, and 10% confidence levels, respectively

disclosures tend to have a more positive effect on SRCs' capital investment when affiliated ownership is higher. Overall, there is inconclusive evidence that affiliated ownership is associated with adverse selection in current SRCs.

## **5. Effects on Efficiency, Competition and Capital Formation**

The final rules may have competitive effects. On one hand, the amendments may reduce the compliance-related costs of newly eligible registrants relative to current SRCs. The amendments may also increase the competitive advantage of the newly eligible registrants relative to non-eligible registrants that compete with them in the product market. However, because there is no clear evidence that scaled disclosures have a significant effect on the growth of current SRCs, we expect these potentially positive competitive effects to be modest. On the other hand, setting any eligibility threshold may create a competitive disadvantage for those registrants that miss eligibility because their public float or revenue is just above the specified threshold, relative to the newly eligible registrants. However, our economic analysis suggests that this potentially negative effect also is likely to be modest.

As discussed above, our empirical analysis suggests that scaled disclosures are unlikely to have a significant negative effect on the overall information environment of SRCs. Thus, we do not expect the amendments to have a significant negative effect on the information efficiency of affected parties. Finally, it is difficult to quantify the effect of scaled disclosures on capital formation. The Commission's 2007 amendments coincided with the 2008 financial crisis and its aftermath, which contributed to extremely thin public capital market activities. The potential cost savings and the potential negative consequences of scaled disclosure for reporting companies discussed in Tables 5 and 6 (based on data encompassing the period during the financial crisis) are modest. These figures do not include potential cost savings from newly-

eligible companies that may contemplate going public.<sup>171</sup>

### **C. Possible Alternatives**

In this section, we present several alternatives to the final rules and discuss their relative costs and benefits.

As a first alternative, we could have used a different registrant size metric in the SRC definition. While public float has the advantage of capturing the value held by non-affiliated investors who may be more affected by informational asymmetries, the disadvantage of public float is twofold. First, reported public float numbers are not easily verifiable. Second, using public float to define eligibility may increase adverse selection due to conflicts of interest between affiliated and non-affiliated owners. We considered equity market value as an alternative size metric to public float. Equity market value is in many instances more accessible and more easily verifiable than public float. It does not as effectively differentiate registrants based on the degree of informational asymmetry concerns, but it also does not favor registrants with more affiliated ownership. If we define registrants as SRCs when they have (1) less than \$250 million in equity market value, (2) no equity market value and revenue below \$100 million, or (3) less than \$700 million in equity market value and revenue below \$100 million, the number of registrants estimated to become eligible for scaled disclosure declines by five percent, relative to the number that are estimated to be eligible under the rule amendments with available 2016 data on public float, revenue and market value. Thus, this alternative would lead to a slightly smaller pool of registrants eligible for SRC status than under the amendments.

As a second alternative, we could have used different thresholds. Neither public float nor revenue data show a natural breakpoint for different thresholds. For example, we could take

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<sup>171</sup> See Section IV.B.1.

inflation since 2007 into account, raising the public float threshold from \$75 million to \$86.2 million and the revenue threshold from \$50 million to \$57.5 million. An inflation adjustment of the current thresholds would expand the pool of eligible SRCs by 83 registrants, 78 of which reported public float of between \$75 million and \$86.2 million in their 2016 Form 10-Ks, and five of which had no public float and revenue of between \$50 million and \$57.5 million.<sup>172</sup>

Alternatively, instead of the \$250 million public float threshold for all registrants and the \$700 million public float threshold for registrants with revenue below \$100 million, we could have allowed the \$700 million public float threshold to apply to all registrants, regardless of revenue. A test capturing all registrants with less than \$700 million in public float, regardless of revenue, would have expanded the pool of eligible SRCs with available data by 1,029 registrants. Because the \$700 million is the threshold in the “large accelerated filer” definition, the effect of this alternative would be to permit all accelerated filers to provide the SRC scaled disclosures.

For registrants with no public float or public float of less than \$700 million, instead of the \$100 million revenue threshold, we could have used a revenue threshold of \$1 billion. A \$1 billion revenue threshold would make scaled disclosure accommodations for SRCs and EGCs generally more consistent for the subset of SRCs that have no public float or public float of less than \$700 million.<sup>173</sup> Using 2016 data, we estimate that if we were to increase the revenue threshold from \$100 million to \$1 billion in addition to the accommodations being adopted, there would be 879 newly eligible registrants based on revenues, in addition to the 966 newly eligible

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<sup>172</sup> The inflation adjustment was performed using the CPI calculator of the Bureau of Labor Statistics (<http://data.bls.gov/cgi-bin/cpicalc.pl>).

<sup>173</sup> An EGC is defined as an issuer that had total annual gross revenues of less than \$1.07 million during its most recently completed fiscal year. Pub. L. No. 112-106, Sec. 101, 126 Stat. 306 (2012); 15 U.S.C. 77b(a)(19); 15 U.S.C. 78c(a)(80). Inflation Adjustments and Other Technical Amendments under Titles I and II of the JOBS Act, Release No. 33-10332 (Mar. 31, 2017) [82 FR 17545 (Apr. 12, 2017)].

registrants under the final rules. Expanding the pool of registrants eligible for SRC status using this alternative revenue threshold would further reduce overall compliance costs for registrants but also potentially increase the informational asymmetries and other adverse effects associated with scaled disclosures. Relative to the current SRCs or the newly eligible SRCs under the final rules, these additional qualifying registrants also may have different characteristics that could affect the appropriateness of scaled disclosure. For example, the 879 additional registrants under this alternative are much larger, implying that any cost savings from scaled disclosures would generate a much smaller impact on the registrants' market value, and may not justify the potential loss of informational transparency.

As a third alternative, we could have considered reducing the number of registrants that our rules define as accelerated filers, which would expand the number of registrants eligible for the Sarbanes-Oxley Act Section 404(b) exemption. The newly eligible SRCs under the final rules will remain accelerated filers and must comply with Section 404(b). This creates two tiers among SRCs. Registrants with public floats below \$75 million are eligible for the scaled disclosures and, as non-accelerated filers, are exempt from Section 404(b). Registrants with either (1) public floats of \$75 million or more and less than \$250 million or (2) public floats of \$75 million or more and less than \$700 million and less than \$100 million in revenues will be eligible only for the scaled disclosures and, as accelerated filers, must comply with Section 404(b). In evaluating the costs and benefits of this alternative, we considered the comments that the Commission received in response to the Proposing Release. In light of these comments, as stated above, the Chairman has directed the staff to formulate recommendations to the Commission for possible changes to reduce the number of registrants that our rules define as accelerated filers.

## V. Paperwork Reduction Act

### A. Background

The final rules will affect existing rules, regulations and forms that contain “collection of information” requirements within the meaning of the Paperwork Reduction Act of 1995 (“PRA”).<sup>174</sup> We are submitting the proposals to the Office of Management and Budget (“OMB”) for review in accordance with the PRA and its implementing regulations.<sup>175</sup> We also requested comment on the changes to these “collection of information” requirements in the Proposing Release.

The titles of the collections of information are:<sup>176</sup>

- (1) “Regulation S-X” (OMB Control No. 3235-0009);
- (2) “Regulation S-K” (OMB Control No. 3235-0071);
- (3) “Regulation C” (OMB Control No. 3235-0074);
- (4) “Regulation 12B” (OMB Control No. 3235-0062);
- (5) “Form 10-K” (OMB Control No. 3235-0063);
- (6) “Form 10-Q” (OMB Control No. 3235-0070);
- (7) “Form 8-K” (OMB Control No. 3235-0060);
- (8) “Regulation 14A and Schedule 14A” (OMB Control No. 3235-0059);
- (9) “Regulation 14C and Schedule 14C” (OMB Control No. 3235-0057);
- (10) “Form 10” (OMB Control No. 3235-0064);

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<sup>174</sup> 44 U.S.C. 3501 *et seq.*

<sup>175</sup> 44 U.S.C. 3507(d); 5 CFR 1320.11.

<sup>176</sup> The paperwork burdens from Regulation S-X, Regulation S-K, Regulation C, and Regulation 12B are imposed through the forms that are subject to the requirements in those regulations and are reflected in the analysis of those forms. To avoid a PRA inventory reflecting duplicative burdens and for administrative convenience, we assign a one-hour burden to each of Regulation S-X, Regulation S-K, Regulation C, and Regulation 12B.



- (11) “Form S-1” (OMB Control No. 3235-0065);
- (12) “Form S-3” (OMB Control No. 3235-0073);
- (13) “Form S-4” (OMB Control No. 3235-0324); and
- (14) “Form S-11” (OMB Control No. 3235-0067).

We adopted the existing rules, regulations, and forms pursuant to the Securities Act and the Exchange Act. These rules, regulations, and forms set forth the disclosure requirements for annual and quarterly reports, proxy and information statements, current reports, and registration statements that are prepared by registrants to provide investors information to make informed investment and voting decisions.

The hours and costs associated with preparing disclosure, filing information required by forms, and retaining records constitute reporting and cost burdens imposed by collection of information requirements. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information requirement unless it displays a currently valid control number. Compliance with the information collections listed above is mandatory to the extent applicable to each registrant.<sup>177</sup> Responses to the information collections are not kept confidential and there is no mandatory retention period for the information disclosed.

## **B. Summary of the Final Amendments**

As described in more detail above, we are adopting final rules to amend the definition of SRC to encompass a greater number of registrants and to revise Rule 3-05(b)(2)(iv) of Regulation S-X to align the revenue threshold in that rule with the new revenue threshold in the definition of SRC. The final rules make scaled disclosure accommodations available to a larger

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<sup>177</sup> As noted above, registrants claiming SRC status have the option to comply with the scaled disclosures available to them on an item-by-item basis.

number of registrants. As a result, the final rules should decrease the disclosure requirements for registrants that fall within the expanded thresholds of the SRC definition and should decrease the disclosure burden for registrants acquiring other companies by increasing the number of acquired companies for which Rule 3-05(b)(2)(iv) of Regulation S-X permits one less year of financial information to be disclosed.

In the Proposing Release, we proposed to amend the SRC definition to include registrants with a public float of less than \$250 million, as well as registrants with annual revenues of less than \$100 million for the previous year and no public float. We are adopting the amendments generally as proposed with two changes. In a change from the proposal, the SRC definition in the final rules also will include registrants with annual revenues of less than \$100 million for the previous year and a public float of less than \$700 million. As detailed below, the burden estimates for the respective forms and schedules have been revised to reflect that the SRC scaled disclosure accommodations also will be available to the additional registrants that come within these revised thresholds.

In another change from the proposal, we are amending Rule 3-05(b)(2)(iv) of Regulation S-X to increase the revenue threshold under which certain registrants may omit from certain registration statements or current reports the earliest of the three fiscal years of audited financial statements of an acquired business or business to be acquired.<sup>178</sup> Accordingly, we have added two new titles, “Regulation S-X” (OMB Control No. 3235-0009) and “Form 8-K” (OMB Control No. 3235-0060), to the collections of information affected by the final rules. The impact of the amendment to Rule 3-05(b)(2)(iv) is reflected in the burden estimates for the applicable

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<sup>178</sup> See note 95.

forms.<sup>179</sup> However, as discussed below, while we estimate that the amendment to Rule 3-05 may decrease the existing paperwork burden for some issuers, we do not believe it will change the total burden estimates for the relevant registration statements and current reports.

The final rules do not change the amount of information required to be included in Exchange Act reports by any registrant because of its status as an accelerated filer or a large accelerated filer.

### **C. Summary of Comment Letters**

One commenter addressed the specific PRA-related comment requests in the Proposing Release.<sup>180</sup> This commenter stated that the proposed adjustment to the SRC definition is fair and that the details provided as the basis for the cost reduction estimates appear to be thorough and specific.<sup>181</sup> As to the ways to enhance the information collected, the commenter stated that the burden of preparing information remained with the respective registrant and that registrants may be required to provide additional disclosure if they are entering into capital transactions.<sup>182</sup> As to ways to minimize the burden of the collection of information, the commenter stated that XBRL may facilitate the evaluation of data.<sup>183</sup> Lastly, the commenter stated that the list of collections of information appeared to be complete and that it was not aware of any collection of information that would be negatively affected.<sup>184</sup>

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<sup>179</sup> See note 176.

<sup>180</sup> See IMA.

<sup>181</sup> *Id.*

<sup>182</sup> *Id.*

<sup>183</sup> *Id.*

<sup>184</sup> *Id.*

#### **D. Revisions to Burden and Cost Estimates**

For purposes of the PRA, the final rules decrease the burden hour and costs estimates for Form 10-K, Form 10-Q, Schedule 14A, Schedule 14C, Form 10, Form S-1, Form S-3, Form S-4, and Form S-11 by approximately 493,016 burden hours and decrease external costs by approximately \$ 66,242,345.<sup>185</sup>

Our burden hour and cost estimates below reflect the average burdens for all registrants that may benefit from the expanded accommodations. In deriving our estimates, we recognize that the burdens likely will vary among individual registrants based on a number of factors, including the size and complexity of their business. We believe that some registrants will experience costs in excess of this average and some registrants will experience less than the average costs.

For quarterly and annual reports and for proxy and information statements, we estimate that 75% of the burden of preparation is carried by the registrant internally and that 25% of the burden is carried by outside professionals retained by the registrant at an average cost of \$400 per hour.<sup>186</sup> For registration statements, we estimate that 25% of the burden of preparation is carried by the registrant internally and that 75% of the burden is carried by outside professionals retained by the registrant at an average cost of \$400 per hour. While we cannot predict with

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<sup>185</sup> These estimates reflect the difference between (1) our estimates of the burden hours and costs for each affected collection of information under the final rules and (2) the current estimates for each affected collection of information prior to effectiveness of the final rules. The current estimates for some of the affected collections of information have changed since the Proposing Release due to changes in our rules that are unrelated to the amendments we are adopting. As a result, our estimated changes in the burden hours and costs for each affected collection of information in this release may differ from our estimates for the same collection of information in the Proposing Release.

<sup>186</sup> We recognize that the costs of retaining outside professionals may vary depending on the nature of the professional services, but for purposes of this PRA analysis, we estimate that such costs will average \$400 per hour. This is the rate we typically estimate for outside legal services used in connection with public company reporting. See Section VI.D below for a discussion of the professional skills needed to comply with the amendments.

certainty the number of newly eligible SRCs that will begin to use the scaled disclosure provisions, for purposes of our PRA calculations, we estimate that 80% of them will do so.<sup>187</sup>

For purposes of the PRA, we estimate that over a three-year period,<sup>188</sup> the annual aggregate decreased burden<sup>189</sup> resulting from the amendments in the final rules will average:

- 403,250 hours and \$53,883,321 of external costs for Form 10-K;
- 88,864 hours and \$11,851,661 of external costs for Form 10-Q;
- 481 hours and \$64,160 of external costs for Schedule 14A;
- 11 hours and \$1,440 of external costs for Schedule 14C;
- nine hours and \$11,163 of external costs for Form 10;
- 145 hours and \$174,000 of external costs for Form S-1;
- 38 hours and \$45,600 of external costs for Form S-3;
- 203 hours and \$243,600 of external costs for Form S-4; and
- 15 hours and \$17,400 of external costs for Form S-11.

## **1. Form 10-K**

We estimate that approximately 966 additional registrants will satisfy the revised definition of a SRC and become eligible to use scaled disclosure in their annual reports on Form

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<sup>187</sup> This estimated realization rate reflects the percentage of registrants eligible to claim SRC status in 2016 that claimed such status. Based on data collected by DERA, 2,408, or approximately 91.2%, of an estimated 2,640 eligible registrants claimed SRC status.

In addition, this estimated realization rate is further reduced to reflect that a portion of newly eligible SRCs may already qualify as EGCs, which are eligible to rely on certain scaled disclosure requirements for a limited period, including some of the scaled requirements available to SRCs. Based on data collected by DERA, 365, or approximately 37.8%, of the 966 registrants in 2016 that would have been newly eligible for scaled disclosure under the final rules were EGCs and therefore already benefitting from a portion of these estimated savings.

<sup>188</sup> We calculated an annual average over a three-year period because OMB approval of PRA submissions covers a three-year period.

<sup>189</sup> Our decreased burden estimates take into account, and are net of, any increased burden that may result from SRCs providing expanded disclosures under disclosure requirements that are more stringent for SRCs than for non-SRCs, such as Item 404 of Regulation S-K.

10-K. These registrants could experience burden and cost savings under the final rules.<sup>190</sup> We estimate that, if all of these registrants used all of the scaled disclosure requirements, they would save an estimated 504,063 burden hours and an aggregate cost of \$67,291,651.<sup>191</sup>

Based on our assumption that 80% of newly eligible registrants will begin to use scaled disclosure, we estimate an aggregate decrease of 403,250 internal burden hours and costs of \$53,833,321 for Form 10-K.<sup>192</sup>

## 2. Form 10-Q

We assume that the same approximately 966 registrants will become newly eligible to use scaled disclosure for purposes of their quarterly reports. We estimate that if all of these registrants used all of the scaled SRC requirements, they would save 111,080 burden hours and an aggregate cost of \$14,814,576.<sup>193</sup>

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<sup>190</sup> We estimate that 966 additional registrants will be eligible under the final rules to use the scaled disclosure requirements available to SRCs for their annual and quarterly reports in the first year. We base this estimate on the number of additional registrants that would have been eligible to use scaled disclosure for their annual and quarterly reports in 2016, based on data collected by DERA from annual reports on Form 10-K filed in 2016. The data show that 779 registrants had a public float of \$75 million or more but less than \$250 million, 26 registrants had no public float and annual revenues of \$50 million or more but less than \$100 million, and 161 registrants had a public float of \$250 million or more but less than \$700 million and annual revenues of less than \$100 million.

<sup>191</sup> Consistent with our analysis in the SRC Adopting Release and the Proposing Release, we estimate the compliance burden for a Form 10-K for a SRC using all scaled disclosure available to be the same as the last available PRA inventory for completing a Form 10-KSB, which was 1,272 burden hours and a cost of \$169,600 (424 professional hours x \$400/hour) per report.

Accordingly, we estimate that, if all eligible registrants used all available scaled disclosure, the final rules would decrease the compliance burden of Form 10-K by up to 504,062.65 hours (1,793.80 internal hours per filing using standard Regulation S-K and Regulation S-X disclosure minus 1,272.00 internal hours per filing using scaled disclosure = 521.80 internal hours saved per filing x 966 filings) and decrease the cost by up to \$67,291,651.41 (598.15 professional hours per filing using standard Regulation S-K and Regulation S-X disclosure minus 424.00 professional hours per filing using scaled disclosure = 174.15 external hours saved per filing x \$400 per hour = \$69,660.09 external cost savings per filing x 966 filings).

<sup>192</sup> This estimated decrease in the compliance burden for Form 10-K is based on 80% x 504,062.65 internal hours saved = 403,250.12 internal hours saved and 80% x \$67,291,651.41 external cost savings = \$53,833,312.13 external cost savings.

<sup>193</sup> Similar to our approach to estimating the reduced compliance burden for a Form 10-K using scaled disclosure, we base our estimates of the reduced compliance burden for SRCs using all scaled disclosure available for certain other filings on the last available PRA inventory for completing the most comparable form under

Assuming that 80% of newly eligible registrants will begin to use scaled disclosure, we estimate an aggregate decrease of 88,864 internal burden hours and costs of \$11,851,661 for Form 10-Q.<sup>194</sup>

### **3. Form 8-K**

We estimate that the amendments to Rule 3-05 may decrease the existing paperwork burden for some registrants but not change the total burden estimates for Form 8-K. This reflects our appraisal that few registrants are eligible to rely on the \$50 million threshold in Rule 3-05(b)(2)(iv) and our expectation that the amendments will not significantly change the number of registrants that are eligible to rely on Rule 3-05(b)(2)(iv).<sup>195</sup> This also is consistent with the Commission's estimate of the impact on the compliance burden for Form 8-K when it revised Rule 3-05 of Regulation S-X in 2007 to increase the threshold in Rule 3-05(b)(iv) from \$25 million to \$50 million.<sup>196</sup>

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Regulation SB. We estimate the compliance burden for a Form 10-Q for a SRC using all scaled disclosure available to be the same as the last available PRA inventory for completing a Form 10-QSB, which was 102.24 burden hours and a cost of \$13,362 (34.08 professional hours x \$400/hour) per report.

Accordingly, we estimate that, if all eligible registrants used all available scaled disclosure, the final rules would decrease the compliance burden of Form 10-Q by up to 111,080.34 hours (140.57 internal hours per filing using standard Regulation S-K disclosure minus 102.24 internal hours per filing using scaled disclosure = 38.33 internal hours saved per filing x 966 registrants x 3 filings per year) and decrease the cost by up to \$14,814,576.00 (46.86 professional hours per filing using standard Regulation S-K disclosure minus 34.08 professional hours per filing using scaled disclosure = 12.78 external hours saved per filing x \$400 per hour = \$5,112 external cost savings per filing x 966 registrants x 3 filings per year).

<sup>194</sup> This estimated decrease in the compliance burden for Form 10-Q is based on  $80\% \times 111,080.34$  internal hours saved = 88,864.27 internal hours saved and  $80\% \times \$14,814,576.00$  external cost savings = \$11,851,660.80 external cost savings.

<sup>195</sup> See Section IV.B.1.

<sup>196</sup> See SRC Adopting Release.

#### **4. Schedule 14A**

We estimate that registrants newly eligible to use scaled disclosure will file approximately 802 definitive proxy statements on Schedule 14A per year.<sup>197</sup> We estimate that if all of these registrants used all of the scaled SRC requirements, they would save 602 burden hours and an aggregate cost of \$80,200.<sup>198</sup>

Assuming that 80% of newly eligible registrants will begin to use scaled disclosure, we estimate an aggregate decrease of 481 internal burden hours and costs of \$64,160 for Schedule 14A.<sup>199</sup>

#### **5. Schedule 14C**

We estimate that registrants newly eligible to use scaled disclosure will file approximately 18 definitive information statements on Schedule 14C per year.<sup>200</sup> We estimate

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<sup>197</sup> We base this estimate on the number of definitive proxy statements on Schedule 14A filed in 2016 by registrants that would have been newly eligible to use scaled disclosure under the final rules. Based on data collected by DERA, registrants with a public float of \$75 million or more but less than \$250 million filed 652 definitive proxy statements on Schedule 14A, registrants with no public float and annual revenues of \$50 million or more but less than \$100 million filed 17 definitive proxy statements on Schedule 14A, and registrants with a public float of \$250 million or more but less than \$700 million and annual revenues of less than \$100 million filed 133 definitive proxy statements on Schedule 14A.

<sup>198</sup> We base our estimate of the reduced compliance burden for Schedule 14A for a SRC using all scaled disclosure available on our estimate of the compliance burden for Item 407(d)(5) and (e)(4) and (5) of Regulation S-K [17 CFR 229.407(d)(5) and (e)(4) and (5)], with which SRCs are not required to comply. We estimate this burden to be 0.75 burden hours and a cost of \$100 (0.25 professional hours x \$400/hour) per report.

Accordingly, we estimate that, if all eligible registrants used all available scaled disclosure, the final rules would decrease the compliance burden of Schedule 14A by up to 601.57 hours (0.75 internal hours saved per filing x 802 filings) and decrease the cost by up to \$80,200.00 (0.25 professional hours saved per filing x \$400 per hour = \$100 external cost savings per filing x 802 filings).

<sup>199</sup> This estimated decrease in the compliance burden for Schedule 14A is based on 80% x 601.57 internal hours saved = 481.25 internal hours saved and 80% x \$80,200.00 external cost savings = \$64,160.00 external cost savings.

<sup>200</sup> We base this estimate on the number of definitive information statements on Schedule 14C filed in 2016 by registrants that would have been newly eligible to use scaled disclosure under the final rules. Based on data collected by DERA, registrants with a public float of \$75 million or more but less than \$250 million filed nine definitive information statements on Schedule 14C, registrants with no public float and annual revenues of \$50 million or more but less than \$100 million filed no definitive information statements on Schedule 14C, and registrants with a public float of \$250 million or more but less than \$700 million and annual revenues of less than \$100 million filed nine definitive information statements on Schedule 14C.



that if all of these registrants used all of the scaled SRC requirements, they would save 14 burden hours and an aggregate cost of \$1,800.<sup>201</sup>

Assuming that 80% of newly eligible registrants will begin to use scaled disclosure, we estimate an aggregate decrease in burden of 11 internal burden hours and costs of \$1,440 for Schedule 14C.<sup>202</sup>

## **6. Form 10**

We estimate that registrants newly eligible to use scaled disclosure will file one registration statements on Form 10 per year.<sup>203</sup> Assuming that this registrant uses all of the scaled SRC requirements, we estimate an aggregate decrease of nine internal burden hours and cost of \$11,163 for Form 10.<sup>204</sup> Due to the low number of Form 10 filers and rounding

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<sup>201</sup> Similar to Schedule 14A, we base our estimate of the decrease in the compliance burden for Schedule 14C for a SRC using all scaled disclosure available on our estimate of the compliance burden for Item 407(d)(5) and (e)(4) and (5) of Regulation S-K, which is 0.75 burden hours and a cost of \$100 (0.25 professional hours x \$400/hour) per report.

Accordingly, we estimate that, if all eligible registrants used all available scaled disclosure, the final rules would decrease the compliance burden of Schedule 14C by up to 13.48 hours (0.75 internal hours saved per filing x 18 filings) and decrease the cost by up to \$1,800.00 (0.25 professional hours saved per filing x \$400 per hour = \$100 external cost savings per filing x 18 filings).

<sup>202</sup> This estimated decrease in the compliance burden for Schedule 14C is based on 80% x 13.48 internal hours saved = 10.79 internal hours saved and 80% x \$1,800 external cost savings = \$1,440 external cost savings.

<sup>203</sup> We generally base our estimated number of each type of registration statement filed on the average number of that type of registration statement filed in each of the calendar years 2014 through 2016 by registrants that would have been newly eligible to use scaled disclosure under the final rules.

Based on data collected by DERA, registrants that would have been newly eligible to use scaled disclosure under the final rules filed an average of less than one registration statement on Form 10 per year during the period 2014 through 2016. However, we believe an estimate of one Form 10 is more reasonable because, as reflected in the Proposing Release, such registrants have filed more than one Form 10 in prior years.

<sup>204</sup> We estimate the compliance burden for a Form 10 for a SRC using all scaled disclosure available to be the same as the last available PRA inventory for completing a Form 10-SB, which was 44.50 burden hours and a cost of \$53,400 (133.50 professional hours x \$400/hour) per report.

Accordingly, if all eligible registrants used all available scaled disclosure, we estimate that the final rules will decrease the compliance burden of Form 10 by up to 9.30 hours (53.80 internal hours per filing using standard Regulation S-K and Regulation S-X disclosure minus 44.50 internal hours per filing using scaled disclosure = 9.30 internal hours saved per filing x one filing) and decrease the cost by up to \$11,163.20 (161.41 professional hours per filing using standard Regulation S-K and Regulation S-X disclosure minus 133.50 professional hours

considerations, we assume that all newly eligible registrants filing Form 10 will begin to use scaled disclosure and therefore realize the full extent of burden and cost savings.

## **7. Form S-1**

We estimate that registrants newly eligible to use scaled disclosure will file approximately 25 registration statements on Form S-1 per year.<sup>205</sup> We estimate that if all of these registrants use all of the scaled SRC requirements, they would save 181 burden hours and an aggregate cost of \$217,500.<sup>206</sup>

Assuming that 80% of these newly eligible registrants will begin to use scaled disclosure, we estimate an aggregate decrease of 145 internal burden hours and costs of \$174,000 for Form S-1.<sup>207</sup>

## **8. Form S-3**

We estimate that registrants newly eligible to use scaled disclosure will file approximately 190 registration statements on Form S-3 per year.<sup>208</sup> We estimate that if all of

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per filing using scaled disclosure = 27.91 external hours saved per filing x \$400 per hour = \$11,163.20 external cost savings per filing x one filing).

<sup>205</sup> Based on data collected by DERA, during 2014 through 2016, registrants with a public float of \$75 million or more but less than \$250 million filed an average of approximately 17 registration statements on Form S-1 each year, registrants with no public float and annual revenues of \$50 million or more but less than \$100 million filed an average of approximately two registration statements on Form S-1 each year, and registrants with a public float of \$250 million or more but less than \$700 million and annual revenues of less than \$100 million filed an average of six registration statements on Form S-1 each year.

<sup>206</sup> We estimate the compliance burden for a Form S-1 for a SRC using all scaled disclosure available to be the same as the last available PRA inventory for completing a Form SB-2, which was 159.50 burden hours and a cost of \$191,400 (478.50 professional hours x \$400/hour) per report.

Accordingly, we estimate that, if all eligible registrants used all available scaled disclosure, the final rules would decrease the compliance burden of Form S-1 by up to 181.25 hours (166.75 internal hours per filing using standard Regulation S-K and Regulation S-X disclosure minus 159.50 internal hours per filing using scaled disclosure = 7.25 internal hours saved per filing x 25 filings) and decrease the cost by up to \$217,500.00 (500.25 professional hours per filing using standard Regulation S-K and Regulation S-X disclosure minus 478.50 professional hours per filing using scaled disclosure = 21.75 external hours saved per filing x \$400 per hour = \$8,700 external cost savings per filing x 25 filings).

<sup>207</sup> This estimated decrease in the compliance burden for Form S-1 is based on 80% x 181.25 internal hours saved = 145.00 internal hours saved and 80% x \$217,500.00 external cost savings = \$174,000.00 external cost savings.

these registrants use all of the scaled SRC requirements, they would save 48 burden hours and an aggregate cost of \$57,000.<sup>209</sup>

Assuming that 80% of the newly eligible registrants will begin to use scaled disclosure, we estimate an aggregate decrease of 38 internal burden hours and costs of \$ 45,600 for Form S-3.<sup>210</sup>

## **9. Form S-4**

We estimate that registrants newly eligible to use scaled disclosure will file approximately 35 registration statements on Form S-4 per year.<sup>211</sup> We estimate that if all of these registrants use all of the scaled SRC requirements, they would save 254 burden hours and an aggregate cost of \$304,500.<sup>212</sup>

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<sup>208</sup> Based on data collected by DERA, during 2014 through 2016, registrants with a public float of \$75 million or more but less than \$250 million filed an average of approximately 148 registration statements on Form S-3 each year, registrants with no public float and annual revenues of \$50 million or more but less than \$100 million filed an average of two registration statements on Form S-3 each year, and registrants with a public float of \$250 million or more but less than \$700 million and annual revenues of less than \$100 million filed an average of 40 registration statements on Form S-3 each year.

<sup>209</sup> We base our estimate of the reduced compliance burden for Form S-3 for a SRC using all scaled disclosure available on our estimate of the average compliance burden for Items 503(d) and 504 of Regulation S-K [17 CFR 229.503(d) and 229.504], which requirements are scaled for SRCs. We estimate the decrease in compliance burden for a registration statement on Form S-3 for a SRC using all scaled disclosure available to be 0.25 burden hours and a cost of \$300 (0.75 professional hours x \$400/hour) per filing.

Accordingly, we estimate that, if all eligible registrants used all available scaled disclosure, the final rules would decrease the compliance burden of Form S-3 by up to 47.50 hours (0.25 internal hours saved per filing x 190 filings) and decrease the cost by up to \$57,000.00 (\$300 external cost savings per filing x 190 filings).

<sup>210</sup> This estimated decrease in the compliance burden for Form S-3 is based on  $80\% \times 47.50$  internal hours saved = 38.00 internal hours saved and  $80\% \times \$57,000.00$  external cost savings = \$45,600.00 external cost savings.

<sup>211</sup> Based on data collected by DERA, during 2014 through 2016, registrants with a public float of \$75 million or more but less than \$250 million filed an average of approximately 30 registration statements on Form S-4 each year, registrants with no public float and revenues of \$50 million or more but less than \$100 million filed an average of approximately one registration statement on Form S-4 each year, and registrants with a public float of \$250 million or more but less than \$700 million and annual revenues of less than \$100 million filed an average of four registration statements on Form S-4 each year.

<sup>212</sup> We estimate the reduction in the compliance burden for Form S-4 for a SRC using all scaled disclosure available to be the same as the reduction in the compliance burden for a Form S-1 for a SRC using all scaled disclosure available as compared to standard Regulation S-K and Regulation S-X disclosure, which was 7.25 burden hours and a cost of \$8,700 (21.75 professional hours x \$400/hour) per report.

Assuming that 80% of newly eligible registrants will begin to use scaled disclosure, we estimate an aggregate decrease of 203 internal burden hours and costs of \$243,600 for Form S-4.<sup>213</sup>

## **10. Form S-11**

We estimate that registrants newly eligible to use scaled disclosure will file approximately two registration statements on Form S-11 per year.<sup>214</sup> Assuming that both of these registrants use all of the scaled SRC requirements, we estimate an aggregate decrease of 15 burden hours and cost of \$17,400 for Form S-11.<sup>215</sup>

Due to the low number of Form S-11 filers and rounding considerations, we assume that both of the newly eligible registrants filing Form S-11 will begin to use scaled disclosure and realize the full extent of burden and cost savings.

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Accordingly, we estimate that, if all eligible registrants used all available scaled disclosure, the final rules will decrease the compliance burden of Form S-4 by up to 253.75 hours (7.25 internal hours saved per filing x 35 filings) and decrease the annual cost by up to \$304,500.00 (\$8,700 external cost savings per filing x 35 filings).

<sup>213</sup> This estimated decrease in the compliance burden for Form S-4 is based on 80% x 253.75 internal hours saved = 203.00 internal hours saved and 80% x \$304,500.00 external cost savings = \$243,600.00 external cost savings.

<sup>214</sup> Based on data collected by DERA, during 2014 through 2016, registrants with a public float of \$75 million or more but less than \$250 million filed an average of approximately one registration statement on Form S-11 each year, registrants with no public float and revenues of \$50 million or more but less than \$100 million filed an average of less than one registration statement on Form S-11 each year, and registrants with a public float of \$250 million or more but less than \$700 million and annual revenues of less than \$100 million filed an average of one registration statement on Form S-11 each year.

<sup>215</sup> We estimate the reduction in the compliance burden for Form S-11 for a SRC using all scaled disclosure available to be the same as reduction in the compliance burden for Form S-1 for a SRC using all scaled disclosure available as compared to standard Regulation S-K disclosure and Regulation S-X, which was 7.25 burden hours and a cost of \$8,700 (21.75 professional hours x \$400/hour) per report.

Accordingly, we estimate that, if both eligible registrants used all available scaled disclosure, the final rules will decrease the compliance burden of Form S-11 by up to 14.50 hours (7.25 internal hours saved per filing x two filings) and decrease the annual cost by up to \$17,400.00 (\$8,700 external cost savings per filing x two filings).

## **VI. Final Regulatory Flexibility Analysis**

The Regulatory Flexibility Act (“RFA”)<sup>216</sup> requires us, in promulgating rules under Section 553 of the Administrative Procedure Act,<sup>217</sup> to consider the impact of those rules on small entities. We have prepared this Final Regulatory Flexibility Analysis (“FRFA”) in accordance with Section 604 of the RFA.<sup>218</sup> This FRFA relates to amendments to the SRC definition as used in our rules and Rule 3-05 of Regulation S-X. An Initial Regulatory Flexibility Analysis (“IRFA”) was prepared in accordance with the RFA and was included in the Proposing Release.

### **A. Need for, and Objectives of, the Final Rules**

The amendments to the SRC definition in the final rules are intended to promote capital formation through a modest reduction in compliance costs and disclosure burdens for these registrants by expanding the number of registrants that qualify as SRCs and are eligible to provide scaled disclosure, while maintaining appropriate investor protections. These amendments will enable a registrant to qualify as a SRC based on a public float test or a revenue test that includes registrants both with and without a public float.<sup>219</sup> We believe that the amendments will permit a broader group of registrants to make scaled disclosure to their investors without significantly detracting from investor protections.

The amendments to Rule 3-05(b)(2)(iv) of Regulation S-X will maintain the consistency of the revenue thresholds in Rule 3-05 and the definition of a SRC. The current revenue threshold in Rule 3-05(b)(2)(iv) was based on the revenue threshold in the SRC definition, and

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<sup>216</sup> 5 U.S.C. 601 *et seq.*

<sup>217</sup> 5 U.S.C. 553.

<sup>218</sup> 5 U.S.C. 604.

<sup>219</sup> *See* Item 10(f)(1)(i) and (ii) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

the final rules maintain this consistency by increasing the revenue threshold in Rule 3-05(b)(2)(iv) to \$100 million. This amendment will enable more registrants to omit the earliest of the three fiscal years of audited financial statements of an acquired business or business to be acquired in certain registration statements and current reports.

The amendments to the accelerated filer and large accelerated filer definitions in Exchange Act Rule 12b-2 maintain the current thresholds at which registrants are subject to accelerated and large accelerated filer disclosure and filing requirements. At this time, we are not raising the accelerated filer public float threshold or modifying the Section 404(b) requirements for registrants.

The need for, and objectives of, the final rules are discussed in more detail in Sections II and IV above.

## **B. Significant Issues Raised by Public Comments**

In the Proposing Release, we requested comment on all aspects of the IRFA, including the number of small entities that would be affected by the proposed amendments, the existence or nature of the potential impact of the proposals on small entities discussed in the analysis, and how to quantify the impact of the proposed amendments. We did not receive any comments specifically addressing the IRFA. We did, however, receive comments from members of the public on matters that could potentially impact small entities. These comments are discussed at length by topic in the corresponding subsections of Section II above.

While many commenters expressed support for the proposed amendments to the SRC definition,<sup>220</sup> commenters also recommended making changes to the proposed rules that would

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<sup>220</sup> See Acorda et al; AMTA; BDO; BIO; CAQ/CII; CONNECT; Coalition; ICBA; MidSouth; Nasdaq; NVCA; NYSE; Seneca; and IMA.

further expand the number of registrants that would qualify as SRCs and would be eligible to rely on the scaled disclosure requirements. For example, many commenters recommended that the Commission allow a revenue test for companies with a public float.<sup>221</sup> Commenters stated that a revenue test would “stimulat[e] innovation and drive business growth,”<sup>222</sup> “ensure that pre-revenue companies are not forced to divert investment funds...from science to compliance,”<sup>223</sup> and help “avoid stifling the advancement of [these] companies that face costly compliance burdens.”<sup>224</sup> Two commenters specifically recommended that the Commission adopt a test based on revenues of less than \$100 million and a public float of less than \$700 million, as recommended by the Small Business Forum.<sup>225</sup> In response to commenters<sup>226</sup> and recommendations from the Small Business Forum,<sup>227</sup> the definition in the final rules will include, in addition to registrants with a public float of less than \$250 million, registrants with annual revenues of less than \$100 million during their most recently completed fiscal year and either no public float or a public float of less than \$700 million.<sup>228</sup> As described above, we believe that it is appropriate to provide a measure by which a registrant with public float but with limited revenues may qualify as a SRC.<sup>229</sup>

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<sup>221</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; CSBA; Nasdaq; NYSE; and Zeller.

<sup>222</sup> BIO.

<sup>223</sup> Acorda, et al.

<sup>224</sup> AMTA.

<sup>225</sup> See BIO; and Calithera.

<sup>226</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; and CSBA.

<sup>227</sup> See notes 16 and 85 for a discussion of the Small Business Forum recommendations.

<sup>228</sup> See Item 10(f)(1)(ii) of Regulation S-K; Securities Act Rule 405; Exchange Act Rule 12b-2.

<sup>229</sup> See Section II.A.2.

We are not, however, adopting a revenue test without a limitation on the public float or market capitalization of the company, as specifically suggested by two commenters.<sup>230</sup> We believe the amended revenue test in the final rules is consistent with the position expressed by these commenters and others<sup>231</sup> that it is not necessary to subject capital-intensive, low-revenue registrants with larger public floats or market capitalizations to the same reporting requirements as registrants with larger public floats and more well-established, revenue-generating businesses. The amended revenue test in the final rules will enable these registrants to benefit from the cost-savings of scaled reporting, while recognizing that as a registrant's business and public float grows, investors should benefit from greater disclosure. The additional information provided by the registrant in these circumstances will assist a growing investor base in making informed investment decisions and should also lead to a lower cost of capital for the business as it grows.

Two commenters recommended amending Rule 3-05 to increase the revenue threshold in paragraph (b)(2)(iv) to \$100 million to maintain the alignment between Rule 3-05 and the definition of a SRC.<sup>232</sup> Given that the current revenue threshold in Rule 3-05(b)(2)(iv) was based on the revenue threshold in the SRC definition<sup>233</sup> and that the final rules, among other things, increase the revenue threshold in the SRC definition from \$50 million to \$100 million, we believe it is appropriate to raise the net revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X from \$50 million to \$100 million.

While some commenters supported eliminating the provision in the accelerated filer and large accelerated filer definitions that specifically excludes registrants that are eligible to use the

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<sup>230</sup> See NYSE; and Nasdaq.

<sup>231</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; CSBA; NYSE; and Nasdaq.

<sup>232</sup> See EY; and BDO.

<sup>233</sup> See 1996 Rule 3-05 Adopting Release and SRC Adopting Release.



SRC disclosure requirements for their annual or quarterly reports,<sup>234</sup> many other commenters recommended that the Commission increase the thresholds in the accelerated filer definition, consistent with the changes to the SRC definition.<sup>235</sup> Commenters recommended increasing the public float threshold in the accelerated filer definition to reduce compliance costs<sup>236</sup> and to maintain consistency in the rules.<sup>237</sup>

The final rules include amendments to the accelerated filer and large accelerated filer definitions in Exchange Act Rule 12b-2 to maintain the current thresholds at which registrants are subject to accelerated and large accelerated filer disclosure and filing requirements. These amendments will change the current relationship between the SRC and “accelerated filer” definitions by allowing a registrant to qualify as both a SRC and an accelerated filer.<sup>238</sup> As stated above, the Chairman has directed the staff to formulate recommendations to the Commission for possible changes to reduce the number of registrants that our rules define as accelerated filers. As part of the staff’s consideration of possible recommended amendments, the Chairman has directed the staff to consider, among other things, the historical and current relationship between the SRC and “accelerated filer” definitions.

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<sup>234</sup> See BDO; CAQ/CII; CFA Institute; Deloitte; and EY.

<sup>235</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; Coalition; CSBA; ICBA; Dixie; MidSouth; Nasdaq; NVCA; NYSE; and Seneca.

<sup>236</sup> See Acorda, et al; AMTA; BIO; Calithera; CONNECT; Coalition; CSBA; ICBA; Dixie; MidSouth; Nasdaq; NVCA; NYSE; and Seneca.

<sup>237</sup> See BIO; Coalition; Nasdaq; NVCA; and NYSE.

<sup>238</sup> In conjunction with these amendments, we also are adopting technical revisions to Securities Act Forms S-1, S-3, S-4, S-8, and S-11 and Exchange Act Forms 10, 10-Q and 10-K. These amendments modify the cover page of the specified forms to remove the parenthetical next to the “non-accelerated filer” definition that states “(Do not check if a smaller reporting company).” After these amendments, a registrant should check all applicable boxes on the cover page addressing, among other things, non-accelerated, accelerated, and large accelerated filer status, SRC status, and emerging growth company status.

We believe that the final rules will reduce disclosure burdens by expanding the number of registrants that will qualify as SRCs and that are eligible to provide scaled disclosure, while maintaining appropriate investor protections.

### **C. Small Entities Subject to the Final Rules**

For purposes of the RFA, under 17 CFR 230.157 (Securities Act Rule 157), an issuer, other than an investment company, is a “small business” or “small organization” if it had total assets of \$5 million or less on the last day of its most recent fiscal year and is engaged or proposing to engage in an offering of securities not exceeding \$5 million. Under 17 CFR 240.0-10(a) (Exchange Act Rule 0-10(a)), an issuer, other than an investment company, is a “small business” or “small organization” if it had total assets of \$5 million or less on the last day of its most recent fiscal year.

We estimate that there are currently 1,181 entities that qualify as “small” under the definitions set forth above.<sup>239</sup> We believe it is likely that virtually all small businesses or small organizations, as defined in our rules described above, are already encompassed within the current SRC definition and the current revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X and will continue to be encompassed within the revised thresholds contained in the final rules. To the extent any small business or small organization, as defined for RFA purposes, is not already encompassed within the current SRC definition and the current revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X, we believe it is likely that the revised thresholds contained in the final rules will capture those entities.

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<sup>239</sup> This estimate is based on staff analysis of XBRL data submitted by filers, excluding co-registrants, with EDGAR filings of Forms 10-K filed during the calendar year of January 1, 2016 to December 31, 2016.

#### **D. Projected Reporting, Recordkeeping and Other Compliance Requirements**

The amendments to the SRC definition in the final rules increase the number of registrants eligible to provide scaled disclosures in response to Regulation S-K and Regulation S-X disclosure requirements. These amendments do not revise the scaled disclosure requirements themselves, but could modestly decrease the disclosures required for registrants that will qualify as SRCs under the expanded thresholds.

Consistent with the amendments to the revenue threshold in the SRC definition, the amendment to Rule 3-05 of Regulation S-X raises the net revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X from \$50 million to \$100 million. Current Rule 3-05(b)(2)(iv) allows certain registrants to omit financial statements of businesses acquired or to be acquired in certain registration statements and current reports for the earliest of the three fiscal years required if the net revenues of the business to be acquired are less than \$50 million. With the amendment, those registrants will become eligible to omit the relevant financial statements for acquired businesses with net annual revenues of \$50 million or more but less than \$100 million in the most recent fiscal year. In this way, the amendment to Rule 3-05 could moderately decrease the existing disclosure requirements for some registrants; however, we do not expect that the number of registrants affected by the amendments will be significant.

Both (i) the amendments to the SRC definition, which expand the number of registrants that qualify for the scaled disclosure based on revenue and public float measures, and (ii) the amendment to Rule 3-05 of Regulation S-X, which expands the pool of acquired companies for which registrants are required to provide only two years of financials, reduce disclosure already required to be prepared under our rules. Accordingly, there are no particular professional skills needed to comply with the amendments themselves. Consistent with the current rules, however,

a registrant will need to monitor the applicable thresholds for disclosure and to comply with the underlying existing disclosure requirements, which may require the use of professional skills, including information technology, accounting, and legal skills.

The amendments are discussed in detail in Section II above. We discuss the economic impact, including the estimated compliance costs and burdens, of the final rules in Section IV (Economic Analysis) and Section V (Paperwork Reduction Act) above.

#### **E. Agency Action to Minimize Effect on Small Entities**

The RFA directs us to consider significant alternatives that would accomplish the stated objectives of the amendments, while minimizing any significant adverse impact on small entities. Accordingly, we considered the following alternatives:

- establishing different compliance or reporting requirements or timetables that take into account the resources available to small entities;
- clarifying, consolidating or simplifying compliance and reporting requirements for small entities under our rules as revised by the amendments;
- using performance rather than design standards; and
- exempting small entities from coverage of all or part of the amendments.

The amendments generally do not create any new compliance or reporting requirements. Instead, the amendments expand the number of companies eligible for the different compliance and reporting requirements available to SRCs and increase the revenue threshold to qualify for the disclosure accommodation in Rule 3-05(b)(2)(iv) of Regulation S-X.<sup>240</sup> As a result, we do not believe it is necessary or appropriate to exempt small entities in connection with this

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<sup>240</sup> As discussed in note 20, Item 404 is the only disclosure item in Regulation S-K that may require more extensive information for SRCs than for non-SRCs. *See also* note 22.

rulemaking. The amendments are intended to increase the number of registrants eligible to provide scaled disclosures under Regulation S-K and Regulation S-X. To the extent any small entity is not already encompassed within the current SRC definition or the current revenue threshold in Rule 3-05(b)(2)(iv) of Regulation S-X, we believe it is likely that the revised thresholds contained in the final rules will capture those entities, thereby enabling them to provide scaled disclosures. Therefore, we believe that the amendments will simplify compliance and reporting requirements for small entities. Small entities may avail themselves of the amendments upon their effective date. This timetable will provide newly-eligible small entities with the ability to take advantage of the scaled disclosure requirements at the earliest possible date. In this regard, we do not believe that it is necessary to establish a different timetable for small entities. With respect to the use of performance rather than design standards, because the amendments are not expected to have any significant adverse effect on small entities (and are, in fact, expected to relieve burdens for some such entities), we do not believe it is necessary to use performance standards in connection with this rulemaking.

In Section IV, above, we discuss additional alternatives that we have considered and their economic impact.<sup>241</sup> We note that those alternatives, such as using a different threshold or different standard for determining SRC status, would be unlikely to have a significant effect on smaller entities because, as noted above, we believe virtually all small entities are already eligible for SRC status. Similarly, with respect to the alternative of not amending the accelerated and large accelerated filer definitions, we believe there are very few small entities that will be

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<sup>241</sup> See Section IV.C. (alternatives include (i) using a different registrant size metric in the SRC definition, (ii) revising the SRC definition using different thresholds, and (iii) reducing the number of registrants that our rules define as accelerated filers, which would expand the number of registrants eligible for the Sarbanes-Oxley Act Section 404(b) exemption).

considered accelerated filers under the definitions in the final rules, and, therefore, this alternative would not significantly affect small entities.<sup>242</sup>

## **VII. Statutory Amendments and Text of Final Rules**

The rule amendments described in this release are being adopted pursuant to Sections 7, 10 and 19 of the Securities Act (15 U.S.C. 77a *et seq.*), as amended, Sections 3(b), 12, 13, 15(d) and 23(a) of the Exchange Act (15 U.S.C. 78a *et seq.*), as amended, and Section 72002 of the FAST Act.

### **List of Subjects in 17 CFR Parts 210, 229, 230, 239, 240, and 249**

Reporting and recordkeeping requirements, Securities.

For the reasons set out in the preamble, the Commission is amending title 17, chapter II of the Code of Federal Regulations as follows:

#### **PART 210 – FORM AND CONTENT OF AND REQUIREMENTS FOR FINANCIAL STATEMENTS, SECURITIES ACT OF 1933, SECURITIES EXCHANGE ACT OF 1934, INVESTMENT COMPANY ACT OF 1940, INVESTMENT ADVISERS ACT OF 1940, AND ENERGY POLICY AND CONSERVATION ACT OF 1975**

1. The authority citation for part 210 continues to read as follows:

**Authority:** 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z-2, 77z-3, 77aa(25), 77aa(26), 77nn(25), 77nn(26), 78c, 78j-1, 78l, 78m, 78n, 78o(d), 78q, 78u-5, 78w, 78ll, 78mm, 80a-8, 80a-20, 80a-29, 80a-30, 80a-31, 80a-37(a), 80b-3, 80b-11, 7202 and 7262, and sec. 102(c), Pub. L. 112-106, 126 Stat. 310 (2012), unless otherwise noted.

2. Amend § 210.3-05 by revising paragraph (b)(2)(iv) to read as follows:

#### **§ 210.3-05 Financial statements of businesses acquired or to be acquired.**

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<sup>242</sup> See Section IV.B.

(b) \* \* \*

(2) \* \* \*

(iv) If any of the conditions exceed 50 percent, the full financial statements specified in §§ 210.3-01 and 210.3-02 shall be furnished. However, financial statements for the earliest of the three fiscal years required may be omitted if net revenues reported by the acquired business in its most recent fiscal year are less than \$100 million.

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**PART 229—STANDARD INSTRUCTIONS FOR FILING FORMS UNDER SECURITIES ACT OF 1933, SECURITIES EXCHANGE ACT OF 1934, AND ENERGY POLICY AND CONSERVATION ACT OF 1975—REGULATION S-K**

3. The authority citation for part 229 continues to read as follows:

**Authority:** 15 U.S.C. 77e, 77f, 77g, 77h, 77j, 77k, 77s, 77z-2, 77z-3, 77aa(25), 77aa(26), 77ddd, 77eee, 77ggg, 77hhh, 77iii, 77jjj, 77nnn, 77sss, 78c, 78i, 78j, 78j-3, 78l, 78m, 78n, 78n-1, 78o, 78u-5, 78w, 78ll, 78mm, 80a-8, 80a-9, 80a-20, 80a-29, 80a-30, 80a-31(c), 80a-37, 80a-38(a), 80a-39, 80b-11, and 7201 *et seq.*, and 18 U.S.C. 1350; sec. 953(b), Pub. L. 111-203, 124 Stat. 1904 (2010); and sec. 102(c), Pub. L. 112-106, 126 Stat. 310 (2012).

\* \* \* \* \*

4. Amend § 229.10 by revising paragraphs (f)(1) and (2) to read as follows:

**§ 229.10 (Item 10) General.**

\* \* \* \* \*

(f) \* \* \* \* \*

(1) *Definition of smaller reporting company.* As used in this part, the term *smaller reporting company* means an issuer that is not an investment company, an asset-backed issuer (as

defined in § 229.1101), or a majority-owned subsidiary of a parent that is not a smaller reporting company and that:

- (i) Had a public float of less than \$250 million; or
- (ii) Had annual revenues of less than \$100 million and either:
  - (A) No public float; or
  - (B) A public float of less than \$700 million.

(2) *Determination.* Whether an issuer is a smaller reporting company is determined on an annual basis.

(i) For issuers that are required to file reports under section 13(a) or 15(d) of the Exchange Act:

(A) Public float is measured as of the last business day of the issuer's most recently completed second fiscal quarter and computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates by the price at which the common equity was last sold, or the average of the bid and asked prices of common equity, in the principal market for the common equity;

(B) Annual revenues are as of the most recently completed fiscal year for which audited financial statements are available; and

(C) An issuer must reflect the determination of whether it came within the definition of smaller reporting company in its quarterly report on Form 10-Q for the first fiscal quarter of the next year, indicating on the cover page of that filing, and in subsequent filings for that fiscal year, whether it is a smaller reporting company, except that, if a determination based on public float indicates that the issuer is newly eligible to be a smaller reporting company, the issuer may choose



to reflect this determination beginning with its first quarterly report on Form 10-Q following the determination, rather than waiting until the first fiscal quarter of the next year.

(ii) For determinations based on an initial registration statement under the Securities Act or Exchange Act for shares of its common equity:

(A) Public float is measured as of a date within 30 days of the date of the filing of the registration statement and computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates before the registration plus, in the case of a Securities Act registration statement, the number of shares of its voting and non-voting common equity included in the registration statement by the estimated public offering price of the shares;

(B) Annual revenues are as of the most recently completed fiscal year for which audited financial statements are available; and

(C) The issuer must reflect the determination of whether it came within the definition of smaller reporting company in the registration statement and must appropriately indicate on the cover page of the filing, and subsequent filings for the fiscal year in which the filing is made, whether it is a smaller reporting company. The issuer must re-determine its status at the end of its second fiscal quarter and then reflect any change in status as provided in paragraph (f)(2)(i)(C) of this section. In the case of a determination based on an initial Securities Act registration statement, an issuer that was not determined to be a smaller reporting company has the option to re-determine its status at the conclusion of the offering covered by the registration statement based on the actual offering price and number of shares sold.

(iii) Once an issuer determines that it does not qualify for smaller reporting company status because it exceeded one or more of the current thresholds, it will remain unqualified unless when making its annual determination either:

- (A) It determines that its public float was less than \$200 million; or
- (B) It determines that its public float and its annual revenues meet the requirements for

subsequent qualification included in the following chart:

Prior Annual Revenues	Prior Public Float	
	None or less than \$700 million	\$700 million or more
Less than \$100 million	Neither threshold exceeded.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$100 million.
\$100 million or more	<b>Public float</b> None or less than \$700 million; and <b>Revenues</b> Less than \$80 million.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$80 million.

Instruction 1 to paragraph (f): A registrant that qualifies as a smaller reporting company under the public float thresholds identified in paragraphs (f)(1)(i) and (f)(2)(iii)(A) of this section will qualify as a smaller reporting company regardless of its revenues.

\* \* \* \* \*

**PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933**

5. The authority citation for part 230 continues to read in part as follows:

**Authority:** 15 U.S.C. 77b, 77b note, 77c, 77d, 77f, 77g, 77h, 77j, 77r, 77s, 77z-3, 77sss, 78c, 78d, 78j, 78l, 78m, 78n, 78o, 78o-7 note, 78t, 78w, 78ll(d), 78mm, 80a-8, 80a-24, 80a-28, 80a-29, 80a-30, and 80a-37, and Pub. L. 112-106, sec. 201(a), sec. 401, 126 Stat. 313 (2012), unless otherwise noted.

\* \* \* \* \*

6. Amend § 230.405 by revising the definition of “smaller reporting company” to read as follows:

**§ 230.405 Definitions of terms.**

\* \* \* \* \*

*Smaller reporting company.* As used in this part, the term *smaller reporting company* means an issuer that is not an investment company, an asset-backed issuer (as defined in § 229.1101 of this chapter), or a majority-owned subsidiary of a parent that is not a smaller reporting company and that:

- (1) Had a public float of less than \$250 million; or
- (2) Had annual revenues of less than \$100 million and either:
  - (i) No public float; or
  - (ii) A public float of less than \$700 million.
- (3) Whether an issuer is a smaller reporting company is determined on an annual basis.
  - (i) For issuers that are required to file reports under section 13(a) or 15(d) of the Exchange Act:
    - (A) Public float is measured as of the last business day of the issuer’s most recently completed second fiscal quarter and computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates by the price at which the common equity was last sold, or the average of the bid and asked prices of common equity, in the principal market for the common equity;

(B) Annual revenues are as of the most recently completed fiscal year for which audited financial statements are available; and

(C) An issuer must reflect the determination of whether it came within the definition of smaller reporting company in its quarterly report on Form 10-Q for the first fiscal quarter of the next year, indicating on the cover page of that filing, and in subsequent filings for that fiscal year, whether it is a smaller reporting company, except that, if a determination based on public float indicates that the issuer is newly eligible to be a smaller reporting company, the issuer may choose to reflect this determination beginning with its first quarterly report on Form 10-Q following the determination, rather than waiting until the first fiscal quarter of the next year.

(ii) For determinations based on an initial registration statement under the Securities Act or Exchange Act for shares of its common equity:

(A) Public float is measured as of a date within 30 days of the date of the filing of the registration statement and computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates before the registration plus, in the case of a Securities Act registration statement, the number of shares of its voting and non-voting common equity included in the registration statement by the estimated public offering price of the shares;

(B) Annual revenues are as of the most recently completed fiscal year for which audited financial statements are available; and

(C) The issuer must reflect the determination of whether it came within the definition of smaller reporting company in the registration statement and must appropriately indicate on the cover page of the filing, and subsequent filings for the fiscal year in which the filing is made, whether it is a smaller reporting company. The issuer must re-determine its status at the end of its

second fiscal quarter and then reflect any change in status as provided in paragraph (3)(i)(C) of this definition. In the case of a determination based on an initial Securities Act registration statement, an issuer that was not determined to be a smaller reporting company has the option to re-determine its status at the conclusion of the offering covered by the registration statement based on the actual offering price and number of shares sold.

(iii) Once an issuer determines that it does not qualify for smaller reporting company status because it exceeded one or more of the current thresholds, it will remain unqualified unless when making its annual determination either:

- (A) It determines that its public float was less than \$200 million; or
- (B) It determines that its public float and its annual revenues meet the requirements for

subsequent qualification included in the following chart:

Prior Annual Revenues	Prior Public Float	
	None or less than \$700 million	\$700 million or more
Less than \$100 million	Neither threshold exceeded.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$100 million.
\$100 million or more	<b>Public float</b> None or less than \$700 million; and <b>Revenues</b> Less than \$80 million.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$80 million.

Instruction 1 to definition of “smaller reporting company”: A registrant that qualifies as a smaller reporting company under the public float thresholds identified in paragraphs (1) and (3)(iii)(A) of this definition will qualify as a smaller reporting company regardless of its revenues.

\* \* \* \* \*

**PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933**

7. The authority citation for part 239 continues to read in part as follows:

**Authority:** 15 U.S.C. 77c, 77f, 77g, 77h, 77j, 77s, 77z-2, 77z-3, 77sss, 78c, 78l, 78m, 78n, 78o(d), 78o-7 note, 78u-5, 78w(a), 78ll, 78mm, 80a-2(a), 80a-3, 80a-8, 80a-9, 80a-10, 80a-13, 80a-24, 80a-26, 80a-29, 80a-30, and 80a-37; and sec. 107, Pub. L. 112-106, 126 Stat. 312, unless otherwise noted.

\* \* \* \* \*

8. Amend Form S-1 (referenced in §239.11) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.” The revisions read as follows:

**Note: The text of Form S-1 does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM S-1**

**REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the

definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

\* \* \* \* \*

9. Amend Form S-3 (referenced in §239.13) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.” The revisions read as follows:

**Note: The text of Form S-3 does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM S-3**

**REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

\* \* \* \* \*

10. Amend Form S-8 (referenced in §239.16b) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.” The revisions read as follows:

**Note: The text of Form S-8 does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM S-8**

**REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>



Emerging growth company

\* \* \* \* \*

11. Amend Form S-11 (referenced in §239.18) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.” The revisions read as follows:

**Note: The text of Form S-11 does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM S-11**

**REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

\* \* \* \* \*

12. Amend Form S-4 (referenced in §239.25) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.” The revisions read as follows:

**Note: The text of Form S-4 does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM S-4**

**REGISTRATION STATEMENT UNDER THE SECURITIES ACT OF 1933**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

\* \* \* \* \*

**PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934**

13. The authority citation for part 240 continues to read in part as follows:

**Authority:** 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78c-3, 78c-5, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78l, 78m, 78n, 78n-1, 78o, 78o-4, 78o-10, 78p, 78q, 78q-1, 78s, 78u-5, 78w, 78x, 78ll, 78mm, 80a-20, 80a-23, 80a-29, 80a-37, 80b-3, 80b-4, 80b-11, 7201 *et seq.*, and 8302; 7 U.S.C. 2(c)(2)(E); 12 U.S.C. 5221(e)(3); 18 U.S.C. 1350; and Pub. L. 111-203, 939A, 124 Stat. 1887 (2010); and secs. 503 and 602, Pub. L. 112-106, 126 Stat. 326 (2012), unless otherwise noted.

\* \* \* \* \*

14. Amend § 240.12b-2 by:

a. In the definition of “accelerated filer and large accelerated filer”:

i. Adding the word “and” at the end of paragraph (1)(ii);

ii. Removing “; and” at the end of paragraph (1)(iii) and in its place adding a period;

iii. Removing paragraph (1)(iv);

iv. Adding the word “and” at the end of paragraph (2)(ii);

v. Removing “; and” at the end of paragraph (2)(iii) and in its place adding a period;

and

vi. Removing paragraph (2)(iv).

b. Revising the definition of “smaller reporting company.” The addition and revision reads as follows:

**§ 240.12b-2 Definitions.**

\* \* \* \* \*

*Smaller reporting company.* As used in this part, the term *smaller reporting company* means an issuer that is not an investment company, an asset-backed issuer (as defined in § 229.1101 of this chapter), or a majority-owned subsidiary of a parent that is not a smaller reporting company and that:

- (1) Had a public float of less than \$250 million; or
- (2) Had annual revenues of less than \$100 million and either:
  - (i) No public float; or
  - (ii) A public float of less than \$700 million.
- (3) Whether an issuer is a smaller reporting company is determined on an annual

basis.

- (i) For issuers that are required to file reports under section 13(a) or 15(d) of the Exchange Act:

- (A) Public float is measured as of the last business day of the issuer's most recently completed second fiscal quarter and computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates by the price at which the common equity was last sold, or the average of the bid and asked prices of common equity, in the principal market for the common equity;

- (B) Annual revenues are as of the most recently completed fiscal year for which audited financial statements are available; and

- (C) An issuer must reflect the determination of whether it came within the definition of smaller reporting company in its quarterly report on Form 10-Q for the first fiscal quarter of the next year, indicating on the cover page of that filing, and in subsequent filings for that fiscal year, whether it is a smaller reporting company, except that, if a determination based on public float

indicates that the issuer is newly eligible to be a smaller reporting company, the issuer may choose to reflect this determination beginning with its first quarterly report on Form 10-Q following the determination, rather than waiting until the first fiscal quarter of the next year.

(ii) For determinations based on an initial registration statement under the Securities Act or Exchange Act for shares of its common equity:

(A) Public float is measured as of a date within 30 days of the date of the filing of the registration statement and computed by multiplying the aggregate worldwide number of shares of its voting and non-voting common equity held by non-affiliates before the registration plus, in the case of a Securities Act registration statement, the number of shares of its voting and non-voting common equity included in the registration statement by the estimated public offering price of the shares;

(B) Annual revenues are as of the most recently completed fiscal year for which audited financial statements are available; and

(C) The issuer must reflect the determination of whether it came within the definition of smaller reporting company in the registration statement and must appropriately indicate on the cover page of the filing, and subsequent filings for the fiscal year in which the filing is made, whether it is a smaller reporting company. The issuer must re-determine its status at the end of its second fiscal quarter and then reflect any change in status as provided in paragraph (3)(i)(C) of this definition. In the case of a determination based on an initial Securities Act registration statement, an issuer that was not determined to be a smaller reporting company has the option to re-determine its status at the conclusion of the offering covered by the registration statement based on the actual offering price and number of shares sold.

(iii) Once an issuer determines that it does not qualify for smaller reporting company status because it exceeded one or more of the current thresholds, it will remain unqualified unless when making its annual determination either:

- (A) It determines that its public float was less than \$200 million; or
- (B) It determines that its public float and its annual revenues meet the requirements for

subsequent qualification included in the following chart:

Prior Annual Revenues	Prior Public Float	
	None or less than \$700 million	\$700 million or more
Less than \$100 million	Neither threshold exceeded.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$100 million.
\$100 million or more	<b>Public float</b> None or less than \$700 million; and <b>Revenues</b> Less than \$80 million.	<b>Public float</b> Less than \$560 million; and <b>Revenues</b> Less than \$80 million.

Instruction 1 to definition of “smaller reporting company”: A registrant that qualifies as a smaller reporting company under the public float thresholds identified in paragraphs (1) and (3)(iii)(A) of this definition will qualify as a smaller reporting company regardless of its revenues.

\* \* \* \* \*

**PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934**

15. The authority citation for part 249 continues to read in part as follows:

**Authority:** 15 U.S.C. 78a *et seq.* and 7201 *et seq.*; 12 U.S.C. 5461 *et seq.*; 18 U.S.C. 1350; Sec. 953(b), Pub. L. 111-203, 124 Stat. 1904; Sec. 102(a)(3), Pub. L. 112-106, 126 Stat.

309 (2012); Sec. 107, Pub. L. 112-106, 126 Stat. 313 (2012), and Sec. 72001, Pub. L. 114-94, 129 Stat. 1312 (2015), unless otherwise noted.

\* \* \* \* \*

16. Amend Form 10 (referenced in §249.210) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.” The revisions read as follows:

**Note: The text of Form 10 does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10**

**GENERAL FORM FOR REGISTRATION OF SECURITIES**

**Pursuant to Section 12(b) or (g) of the Securities Exchange Act of 1934**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

Emerging growth company

\* \* \* \* \*

17. Amend Form 10-Q (referenced in §249.308a) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.” The revisions read as follows:

**Note: The text of Form 10-Q does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

\* \* \* \* \*



18. Amend Form 10-K (referenced in §249.310) by revising the text and check boxes on the cover page immediately before the text “If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.” The revisions read as follows:

**Note: The text of Form 10-K does not, and this amendment will not, appear in the Code of Federal Regulations.**

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K**

\* \* \* \* \*

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

\* \* \* \* \*

By the Commission.

Dated: June 28, 2018.

Brent J. Fields,  
Secretary.