

July 5, 2018

SEC Broadens Definition of “Smaller Reporting Company” and Requires Inline XBRL in Certain Filings

On June 28, the SEC voted on several final rules and rule proposals, including the adoption of final rules that broaden the definition of “smaller reporting company” (available [here](#)) and that require the use of the Inline XBRL format in certain operating company and mutual fund filings (available [here](#)). Both final rules were adopted largely in the form originally proposed.

Broadened Definition of “Smaller Reporting Company”

The SEC established the smaller reporting company (“SRC”) category of companies in 2008 in an effort to reduce the disclosure burden for smaller companies. SRCs may provide more limited, or “scaled,” disclosure under Regulation S-K and Regulation S-X, including:

- The provision of more limited disclosure regarding certain items, such as Description of Business, Executive Compensation and MD&A;
- The omission of certain other items, such as Selected Financial Data and Quantitative and Qualitative Disclosures About Market Risk; and
- The provision of two rather than three years of financial statements.

The new smaller reporting company definition, initially proposed in June 2016, allows a company with less than \$250 million of public float to take advantage of the scaled disclosure accommodations, as compared to the \$75 million threshold under the prior definition. The final rules also expand the definition of SRC to include companies with less than \$100 million in annual revenues during their most recently completed fiscal year if they also have either no public float or a public float of less than \$700 million. Previously, the revenue test required no public float and less than \$50 million in annual revenues. In the adopting release, the SEC stated that it was persuaded by commenters’ suggestions that it is appropriate to provide a measure by which a company with a public float but limited revenues may qualify as an SRC and noted that it will enable some additional capital-intensive, low-revenue companies to benefit from the cost savings of scaled reporting.

The expanded definition of SRC is designed to increase the number of companies able to take advantage of the SRC disclosure accommodations. The SEC estimates that almost 1,000 additional companies will be eligible for SRC status in the first year under the new definition.

Qualification for SRC Status for Companies Initially Unable to Qualify. Consistent with the previous definition, under the revised definition a company that is unable to qualify as an SRC under the initial thresholds will remain unqualified until it determines that it meets one or more lower SRC subsequent qualification thresholds. The subsequent qualification thresholds are 80% of the initial qualification thresholds, *i.e.*, less than \$200 million public float, or less than \$560 million of public float (or no public float) and less than \$80 million of annual revenues. The SEC believes that these lower thresholds are necessary to avoid situations in which companies frequently enter and exit SRC status due to small fluctuations in their public float.

Accelerated and Large Accelerated Filer Status. Contrary to the recommendations of numerous commenters on the proposed rules, the final rules preserve the application of the current thresholds contained in the “accelerated filer” and “large accelerated filer” definitions in Exchange Act Rule 12b-2. As a result, companies with \$75 million or more of public float that qualify as SRCs will remain subject to the requirements that apply to accelerated filers, including the timing of the filing of periodic reports and the requirement that accelerated filers provide the auditor attestation of management’s assessment of internal control over financial reporting required by Section 404(b) of the Sarbanes-Oxley Act. However, the adopting release notes that Chairman Clayton has directed the staff to formulate recommendations for possible additional changes to the “accelerated filer” definition that, if adopted, would have the effect of reducing the number of companies that qualify as accelerated filers.

Acquired Businesses. In a change from the proposed rules, Rule 3-05(b)(2)(iv) of Regulation S-X, which sets forth the requirements for financial statements of businesses acquired or to be acquired in certain registration statements and current reports, has been amended to increase the net revenue threshold in that rule from \$50 million to \$100 million. As a result, companies may omit financial statements of businesses acquired or to be acquired for the earliest of the three fiscal years otherwise required by Rule 3-05 if the net revenues of that business are less than \$100 million.

Required Use of Inline XBRL in Certain Filings

The SEC also voted to adopt amendments, initially proposed in March 2017, to the eXtensible Business Reporting Language (“XBRL”) requirements for operating companies and funds. The amendments require the use of the Inline XBRL format for the submission of operating company financial statement information and fund risk/return summary information. Inline XBRL, currently used voluntarily by a number of operating company filers, involves embedding XBRL data directly into the filing so that the disclosure document is both human-readable and machine-readable, eliminating the need to tag a copy of the information in a separate XBRL exhibit. While the amendments modify existing XBRL requirements, they do not change the categories of filers or scope of disclosures subject to XBRL requirements.

The new Inline XBRL requirements apply to all operating companies, including emerging growth companies, smaller reporting companies and foreign private issuers that provide their financial statements in accordance with U.S. GAAP or IFRS as issued by the International Accounting Standards Board.

In adopting these requirements, the SEC noted that the use of Inline XBRL would, among other things, reduce XBRL preparation time and effort, give the preparer full control over the presentation of XBRL disclosures within the HTML filing, reduce the likelihood of inconsistencies between HTML and XBRL filings and enhance the usability of structured disclosures for investors, who would no longer have to view the XBRL data separately from the text of the documents.

Operating companies that are currently required to submit financial statement information in XBRL will be required to transition to Inline XBRL on a phased basis as follows:

- Large accelerated filers that use U.S. GAAP will be required to comply beginning with fiscal periods ending on or after June 15, 2019.
- Accelerated filers that use U.S. GAAP will be required to comply beginning with fiscal periods ending on or after June 15, 2020.
- All other filers, including foreign private issuers, will be required to comply beginning with fiscal periods ending on or after June 15, 2021.
- Domestic filers will be required to comply beginning with their first Form 10-Q filed for a fiscal period ending on or after the applicable compliance date, as opposed to the first filing for a fiscal period ending on or after that date, to enable filers to gain experience with Inline XBRL through less complex filings.

The requirement that operating companies and funds post XBRL data on their websites will be eliminated upon the effective date of the amendments.

The final rules will become effective 60 days after publication in the Federal Register.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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