Client Alert | US Public Company Advisory / Capital Markets

New and Proposed Rules on Smaller Reporting Companies, XBRL and Whistleblower Program

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On June 28, 2018, the Securities and Exchange Commission ("SEC") approved several final rules and rule proposals that together represent material progress toward many SEC priorities.

Change to the Definition of "Smaller Reporting Company"

The SEC unanimously voted to amend the definition of "smaller reporting company" ("SRC") to allow more companies to take advantage of the scaled disclosures permitted for companies that meet the definition (see Appendix A for the complete list of scaled disclosure requirements applicable to SRCs).[1] Most significantly, the amendments raise the SRC cap to less than $250 million in public float and include as SRCs companies with less than $100 million in annual revenues if they also have either (i) no public float or (ii) a public float that is less than $700 million.[2]

The following table summarizes the amendments to the SRC definition:

Criteria	Previous SRC Definition	Revised SRC Definition
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 • no public float, or • public float of less than $700 million

The change is intended to promote capital formation and reduce compliance costs.

1 The final rule can be found here.

2 Under the new definition, a registrant that determines that it does not qualify as an SRC remains unqualified until it hits caps set at 80 percent of the initial qualification caps, i.e., until it determines that its public float is less than $200 million or, under the revenue test, until it had annual revenues of less than $80 million during its previous fiscal year, 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. This structure is designed to avoid situations in which companies enter and exit SRC status due to small fluctuations in their public float or revenues.

The SEC also approved conforming amendments to the definition of "accelerated filer" in Rule 12b-2 under the Exchange Act to provide that notwithstanding the fact that companies with $75 million or more of public float may now qualify as SRCs, such companies will remain subject to the requirements applicable to accelerated filers, including the accelerated timing of filing of periodic reports and the requirement to provide an auditor's internal control attestation under Section 404(b) of the Sarbanes-Oxley Act. In light of the SRC amendments, SEC Chair Clayton directed the staff to make recommendations for possible additional changes to the definition of "accelerated filer" to reduce the number of companies that qualify as accelerated filers in order to promote capital formation by reducing compliance costs for those companies.

Mandatory Inline eXtensible Business Reporting Language ("XBRL")

As part of its disclosure modernization initiative, the SEC voted to adopt rules mandating the use of Inline XBRL (data tagging embedded directly in the text of an HTML document) for the submission of financial statement information for operating companies, rather than the current format in which XBRL data is provided solely as exhibits to company filings.[3] Filings will also include an exhibit containing contextual information about the XBRL tags embedded in the filing. The new rules also eliminate the requirement for filers to post XBRL exhibits on their websites.

The amendments do not change the categories of filers or scope of disclosures subject to XBRL requirements.

The amendments are intended to improve the data's usefulness, timeliness, and quality. The amendments are also intended to decrease, over time, the cost of preparing the data for submission to the SEC.

The new rules for Inline XBRL will have a three-year phase-in as follows:[4]

- For large accelerated filers that use US GAAP, compliance will be required beginning with fiscal periods ending on or after June 15, 2019.
- For accelerated filers that use US GAAP, compliance will be required beginning with fiscal periods ending on or after June 15, 2020.
- For all other filers, compliance will be required beginning with fiscal periods ending on or after June 15, 2021.

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. Early compliance is permitted; however, EDGAR is not expected to be ready to process Inline XBRL until March 2019. Operating companies may also continue to voluntarily submit certain required filings under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), in Inline XBRL pursuant to an exemptive order issued by the SEC in July 2016.[5] The elimination of the website posting requirement is effective 30 days after publication of the amendments in the Federal Register.

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3 The final rule can be found here.

4 Funds that are currently required to submit risk/return summary information in XBRL will be required to transition to Inline XBRL as follows:

- Large fund groups (net assets of $1 billion or more as of the end of their most recent fiscal year) will be required to comply two years after the effective date of the amendments.
- All other funds will be required to comply three years after the effective date of the amendments.

5 Order Granting Limited and Conditional Exemption under Section 36(a) of the Securities Exchange Act of 1934 from Compliance with Interactive Data File Exhibit Requirement in Forms 6-K, 8-K, 10-Q, 10-K, 20-F, and 40-F to Facilitate Inline Filing of Tagged Financial Data, Release No. 34-78041 (Jun. 13, 2016) [81 FR 39741], permitting operating companies that comply with certain conditions to file structured financial statement data required in their periodic and current reports using Inline XBRL through March 2020, in lieu of filing all their XBRL data in a separate exhibit.

Resulting Changes to Cover Pages of Registration Statements and Periodic Reports

The new SRC rules include conforming amendments to the cover pages for registration statements on Forms S-1, S-3, S-4, S-8, S-11 and Form 10 and periodic reports on Forms 10-K and 10-Q, reflecting the higher threshold for SRC status but the unchanged "accelerated filer" definition. The referenced forms have been revised as follows:

> 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 [ ] (~~Do not check if a smaller reporting company~~)
>
> Smaller reporting company [ ]
>
> Emerging growth company [ ]

In addition, the new Inline XBRL rules include conforming amendments to the cover pages for certain periodic reports, including Forms 10-K and 10-Q, to eliminate references to compliance with the website posting requirement.

The cover pages of Forms 10-K and 10-Q have been revised as follows:

> Indicate by check mark whether the registrant has submitted electronically ~~and posted on its corporate Web site, if any,~~ every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit ~~and post~~ such files).

The changes related to the new SRC rules are effective 60 days from publication in the Federal Register. While there is a phase in period for required use of Inline XBRL, the elimination of the website posting requirements and the related changes to the cover page are effective 30 days after publication of the amendments in the Federal Register and therefore may affect the upcoming second quarter of 2018 Form 10-Q filings for calendar year-end issuers.

Proposed Changes to the SEC's Whistleblower Program

The SEC voted to propose amendments to the rules related to its whistleblower program.[6] The amendments are designed to provide the SEC with additional tools in making awards under the program to ensure that credible whistleblowers are adequately incentivized, increase efficiencies in the claim review process and modify the requirements for anti-retaliation protection to conform to the Supreme Court's recent decision in *Digital Realty v. Somers*.

The proposed changes include:

- *Adjusting Who is Eligible for an Award:*
    - Allowing awards based on money collected under deferred and non-prosecution agreements entered into by the Department of Justice ("DOJ"), a state attorney general in a criminal case, or an SEC settlement agreement entered into outside of a judicial or administrative proceeding addressing violations of the securities laws (to ensure whistleblowers are not disadvantaged because of the particular form of an action that the SEC, DOJ, or state attorney general may elect to pursue).
    - Eliminating potential double recovery under different whistleblower programs by amending the definition of "related action".

6 The proposed rule can be found here.

- *Discretion to Adjust Monetary Awards*:
    - Given the prevalence of awards under US$2 million, vesting the SEC with discretion to adjust awards up to US$2 million (subject to the 30 percent statutory maximum of the total monetary sanctions) in order to encourage tips that might not otherwise qualify for a sufficiently attractive reward and therefore might not appropriately incentivize potential whistleblowers.
    - For awards linked to tips that would result in sanctions of at least US$100 million, vesting the SEC with discretion to adjust awards downwards where a potential award would exceed an amount necessary to promote the program's objectives (subject to the statutory minimum of 10 percent of the total monetary sanctions and in no event below US$30 million).
- *Amending the Definition of "Whistleblower" and Other Digital Reality Conforming Changes:*
    - In *Digital Realty*, the Supreme Court held that the Dodd-Frank anti-retaliation provision only protects a whistleblower who reports a possible securities law violation to the SEC, not internally to the company.[7] The proposed rule would modify Rule 21F-2 under the Exchange Act to establish a uniform definition of "whistleblower" that would apply to all aspects of Section 21F of the Exchange Act. Separately, for purposes of protection against retaliation, an individual would be required to report information about possible securities laws violations to the SEC "in writing" to qualify for the anti-retaliation provisions of Dodd-Frank Act. The rule would retain the requirement that for award eligibility or to obtain heightened confidentiality protection, the whistleblower must submit information on Form TCR or through the SEC's online tips portal.
- *Increasing Efficiency:*
    - Clarifying the SEC's authority to bar individuals based on past behaviors, such as those who submit false information or who make repeated frivolous claims, and providing the SEC with a summary disposition procedure for certain types of "likely denials," such as untimely applications, non-compliant submissions or where the claimant's information was not used.

[7] For more information on the decision in Digital Realty v. Somers, see our previous alert, "Supreme Court Limits Scope of Anti-Retaliation Protections for Whistleblowers Under Dodd-Frank".

Appendix A[8]

Regulation S-K	
Item	**Scaled Disclosure Accommodation**
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 Stockholder Matters	Stock performance graph not required.
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: • Compensation discussion and analysis (CD&A). • Grants of plan-based awards table. • Option exercises and stock vested table. • Pension benefits table. • Nonqualified deferred compensation table. • Disclosure of compensation policies and practices related to risk management. • Pay ratio disclosure.
404 – Transactions with Related Persons, Promoters and Certain Control Persons[9]	Description of policies/procedures for the review, approval or ratification of related party transactions. not required.

[8] 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)].

[9] 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 percent 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.

Regulation S-K	
Item	**Scaled Disclosure Accommodation**
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.

Regulation S-X	
Rule	**Scaled Disclosure Accommodation**
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 requirements regarding the age of financial statements.

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