

Technical Line

SEC – Financial reporting development

Movin' on up to accelerated filer status: You'll need an audit of ICFR for this year

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What you need to know

- ▶ Companies that are now transitioning to accelerated filer status will need an audit of their internal control over financial reporting (ICFR) for this year and must meet accelerated deadlines for financial reporting for their upcoming Form 10-K.
- ▶ A registrant that ceases to be an emerging growth company (EGC) at any point during a fiscal year must obtain an audit of its ICFR for that year, unless it is a non-accelerated filer.

Overview

With the increase in stock prices this year, more public companies are making the transition to a filing status that requires them to obtain audits of their ICFR under Section 404(b) of the Sarbanes-Oxley Act of 2002 (the Act) and meet accelerated deadlines for financial reporting.

Rule 12b-2 of the Exchange Act (Rule 12b-2) requires registrants to reassess their filing status as of the end of each fiscal year based on certain criteria, including their public float as of the last business day of their second fiscal quarter.

As a result, many non-accelerated filers will be required to transition to accelerated filer status beginning with their Form 10-K for the current fiscal year. If that happens, the requirement to obtain auditor attestation about the effectiveness of their ICFR under Section 404(b) of the Act will kick in. Emerging growth companies (EGCs), a new category of issuer created by the Jumpstart Our Business Startups Act of 2012 (JOBS Act), are exempt from the Section 404(b) requirement, even if they become accelerated filers.

This publication discusses the transition from a Section 404(b) exemption and the timing of compliance with this provision of the Act.



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Background

Item 308 of Regulation S-K, *Internal control over financial reporting*, incorporates the internal control reporting provisions of Section 404 of the Act into Securities and Exchange Commission (SEC) regulations. Item 308(a), comprising Section 404(a) of the Act, requires registrants to provide a report by management assessing the effectiveness of the company's ICFR beginning with their second annual report after becoming a public company. Item 308(b) of Regulation S-K requires each annual report of an accelerated filer or a large accelerated filer to include an attestation report from the registrant's independent registered public accounting firm on the registrant's ICFR.

Certain registrants are exempt from complying with the attestation requirement of Section 404(b). New public companies are not required to comply with Section 404 until their second annual report. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 permanently exempted non-accelerated filers from complying with Section 404(b). The JOBS Act allows EGCs to defer compliance with Section 404(b).

The chart below summarizes the Section 404(b) requirements.

Filer status	EGC vs. Non-EGC	Required to comply with Section 404(b)?
Non-accelerated filer	EGC or Non-EGC	No*
Accelerated filer	EGC	No*
	Non-EGC	Yes
Large accelerated filer	N/A	Yes

* Such companies may voluntarily comply with Section 404(b).

As a reminder, the public float thresholds are:

- \$700 million for large accelerated filers
- \$75 million for accelerated filers
- Less than \$75 million for non-accelerated filers¹

See Section 2 and Section 9 of our [2012 SEC annual reports – Form 10-K](#) publication (SCORE No. CC0360) for all of the criteria for each category of filer.

When to comply with Section 404(b) following a transition

Non-accelerated to accelerated or large accelerated filer

When a non-accelerated filer meets all of the criteria in Rule 12b-2 to be an accelerated filer or a large accelerated filer as of the end of its fiscal year, its Form 10-K for that fiscal year will be due on an accelerated basis. As an accelerated or large accelerated filer, the registrant also is required to comply with Section 404(b) in that Form 10-K.

Assume, for example, that a calendar-year company called Deluxe Apartments REIT filed its 2012 Form 10-K as a non-accelerated filer and did not have its auditor attest to the effectiveness of ICFR. Also assume that on 30 June 2013, Deluxe Apartments REIT's public float had increased to \$80 million, and as of 31 December 2013, it met the criteria of an accelerated filer. The registrant's 2013 Form 10-K will be due 17 March 2014 (76 days after year-end because the 75th day is a Sunday) and must include its auditor's report on the effectiveness of ICFR as of 31 December 2013.

A company that loses EGC status must comply with Section 404(b) for the fiscal year in which that status is lost.

Smaller reporting company to accelerated or large accelerated filer

When a registrant that has previously reported as a smaller reporting company (SRC) no longer meets the SRC criteria, Item 10(f)(2)(i) of Regulation S-K delays compliance with “larger reporting company” disclosure provisions until the subsequent fiscal year’s first Form 10-Q. Assume, for example, that a calendar-year public company called Jefferson Co. has been an SRC but did not meet the SRC criteria at 30 June 2013 due to an increase in its public float above \$75 million. Jefferson Co. may continue to provide scaled SRC-level disclosures in its 2013 Form 10-K and would not be required to provide “larger reporting company” disclosures until its Form 10-Q for the first quarter of 2014.

Such a company, however, would need to comply with the Section 404(b) requirements and accelerated reporting deadlines in its Form 10-K for 2013. While this situation isn’t addressed in Regulation S-K, the SEC staff said in guidance in Exchange Act Rule [Compliance and Disclosure Interpretation \(C&DI\) 130.04](#) that a registrant that no longer qualifies as an SRC would be considered an accelerated filer as of the end of that fiscal year. Relief from Section 404(b) is related to a registrant’s filer status and not whether it qualifies for SRC disclosures. Therefore, Item 308(b) of Regulation S-K would require the registrant to comply with Section 404(b).

In our example, while Jefferson Co. could provide SRC-level disclosures in its 2013 Form 10-K, the report would be due 17 March 2014 and must include its auditor’s report on the effectiveness of ICFR as of 31 December 2013.

Exiting EGC status

Emerging growth companies represent a new category of issuer, not a new filing status. They are allowed to elect exemptions from certain requirements and can provide scaled disclosures under the JOBS Act. An EGC therefore could be either a non-accelerated or accelerated filer (large accelerated filers are not eligible to be EGCs). An EGC also could qualify as an SRC.

One of the accommodations the JOBS Act provided for EGCs allows them to defer Section 404(b) requirements. When a registrant loses its EGC status, it must comply with the requirements of Section 404(b), unless it is a non-accelerated filer and therefore exempt from Section 404(b) as described above. An EGC may lose its status as an EGC in any of the following four ways:

- Exceeding \$1 billion in annual revenues
- Issuing more than \$1 billion in nonconvertible debt securities over a rolling three-year period, including securities issued in registered or unregistered offerings
- Becoming a large accelerated filer (i.e., a seasoned issuer with public float of \$700 million or more)
- Hitting the last day of the fiscal year in which it celebrates the fifth anniversary of its first sale of registered common equity securities

A registrant that loses EGC status would be required to file its annual report for that year as a non-EGC. For example, if a calendar-year EGC called Eastside Inc. exceeds \$1 billion in annual revenue in 2013, the EGC relief provisions would not apply to its 2013 Form 10-K. This means Eastside Inc. would have to comply with Section 404(b) in its 2013 Form 10-K, unless it is a non-accelerated filer.

How we see it

- ▶ Registrants that have been exempt from Section 404(b) requirements should closely monitor their public float (and EGC criteria, if applicable) and proactively plan to comply with the Section 404(b) requirements and the accelerated reporting deadlines if necessary this year.

Endnote:

- ¹ Many non-accelerated filers also meet the smaller reporting company criteria included in Item 10(f)(1) of Regulation S-K.

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