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# SEC Guidance On Proxy Presentation Of Certain Matters In The Merger And Acquisition Context

The following is written by Laura Anthony, Esq., a going public attorney focused on OTC listing requirements, direct public offerings, going public transactions, reverse mergers, Form 10 and Form S-1 registration statements, SEC compliance and OTC Market reporting requirements.

On September 23, 2015, the SEC Advisory Committee on Small and Emerging Companies (the "Advisory Committee") met and finalized its recommendation to the SEC regarding changes to the disclosure requirements for smaller publicly traded companies.

By way of reminder, the Committee was organized by the SEC to provide advice on SEC rules, regulations and policies regarding "its mission of protecting investors, maintaining fair, orderly and efficient markets and facilitating capital formation" as related to "(i) capital raising by emerging privately held small businesses and publicly traded companies with less than $250 million in public market capitalization; (ii) trading in the securities of such businesses and companies; and (iii) public reporting and corporate governance requirements to which such businesses and companies are subject."

The topic of disclosure requirements for smaller public companies under the Securities Exchange Act of 1934 ("Exchange Act") has come to the forefront over the past year. In early December the House passed the Disclosure Modernization and Simplification Act of 2014, but the bill was never passed by the Senate and died without further action.

In March of this year the American Bar Association submitted its second comment letter to the SEC making recommendations for changes to Regulation S-K. For a review of these recommendations see my blog Here.

**The Advisory Committee discussed the topic at its meetings on June 3, 2015 and again on July 15, 2015 before finalizing its recommendations, which were published on September 23, 2015. In formulating its recommendations, the Advisory Committee gave specific consideration to the following facts:**

- The SEC has provided for simplified disclosure for smaller reporting companies for over 30 years. Under the current rules a "smaller reporting company" is defined as one that, among other things, has a public float of less than $75 million in common equity, or if unable to calculate the public float, has less than $50 million in annual revenues. Similarly, a company is considered a non-accelerated filer if it has a public float of less than $75 million as of the last day of the most recently completely second fiscal quarter.
- The JOBS Act, enacted on April 5, 2012, created a new category of company called an "emerging growth company" for which certain scaled-down disclosure requirements apply for up to 5 years after an initial IPO. An emerging growth company is one that has total annual gross revenues of less than $1 billion during its most recent completed fiscal year.
- Emerging growth companies are provided with a number of other accommodations with respect to disclosure requirements that would also be beneficial to smaller reporting companies.

**The Advisory Committee then made the following specific recommendations:**

- The SEC should revise the definition of "smaller reporting company" to include companies with a public float of up to $250 million. This will increase the class of companies benefitting from a broad range of benefits to smaller reporting companies, including (i) exemption from the pay ratio rule; (ii) exemption from the auditor attestation requirements; and (iii) exemption from providing a compensation discussion and analysis.
- The SEC should revise its rules to align disclosure requirements for smaller reporting companies with those for emerging growth companies. These include (i) exemption from the requirement to conduct shareholder advisory votes on executive compensation and on the frequency of such votes; (ii) exemption from rules requiring mandatory audit firm rotation; (iii) exemption from pay versus performance disclosure; and (iv) allow compliance with new accounting standards on the date that private companies are required to comply.
- The SEC should revise the definition of "accelerated filer" to include companies with a public float of $250 million or more but less than $700 million. As a result, the auditor attestation report under Section 404(b) of the Sarbanes Oxley Act would no longer apply to companies with a public float between $75 million and $250 million.
- The SEC should exempt smaller reporting companies from XBRL tagging; and
- The SEC should exempt smaller reporting companies from filing immaterial attachments to material contracts.

**My Thoughts**

I completely agree with the recommendations. The disclosure rules are complicated, and compliance is expensive. Moreover, the numerous new rules related to executive compensation including pay ratio, say on pay, pay vs. performance, executive clawback and compensation disclosure and analysis are a huge deterrent for companies that currently do not qualify as a smaller reporting company, but are still small in today's financial world. These companies need an opportunity to grow and generate jobs while still providing meaningful disclosure to the marketplace and investors. The proposed changes in the definition of smaller reporting company to a much more modern reasonable $250 million will greatly assist in that regard.

I especially applaud the recommendation related to XBRL tagging. I firmly believe it is an analytic tool that is not used at all by smaller reporting companies or the small cap marketplace.

**Refresher on Public Company Reporting Requirements**

A public company with a class of securities registered under either Section 12 or which is subject to Section 15(d) of the Securities Exchange Act of 1934, as amended ("Exchange Act") must file reports with the SEC ("Reporting Requirements"). The underlying basis of the Reporting Requirements is to keep shareholders and the markets informed on a regular basis in a transparent manner. Reports filed with the SEC can be viewed by the public on the SEC EDGAR website. The required reports include an annual Form 10-K, quarterly Form 10Q's and current periodic Form 8-K, as well as proxy reports and certain shareholder and affiliate reporting requirements.

A company becomes subject to the Reporting Requirements by filing an Exchange Act Section 12 registration statement on either Form 10 or Form 8-A. A Section 12 registration statement may be filed voluntarily or per statutory requirement if the issuer's securities are held by either (i) 2,000 persons or (ii) 500 persons who are not accredited investors and where the issuer's total assets exceed $10 million. In addition, companies that file a Form S-1 registration statement under the Securities Act of 1933, as amended ("Securities Act") become subject to Reporting Requirement; however, such obligation becomes voluntary in any fiscal year at the beginning of which the company has fewer than 300 shareholders.

A reporting company also has record-keeping requirements, must implement internal accounting controls and is subject to the Sarbanes-Oxley Act of 2002, including the CEO/CFO certifications requirements, prohibition on officer and director loans, and independent auditor requirements. Under the CEO/CFO certification requirement, the CEO and CFO must personally certify the content of the reports filed with the SEC and the procedures established by the issuer to report disclosures and prepare financial statements. For more information on that topic, see my blog Here.

All reports filed with the SEC are subject to SEC review and comment and, in fact, the Sarbanes-Oxley Act requires the SEC to undertake some level of review of every reporting company at least once every three years.

The following are the reports that generally make up a public company's reporting requirements and which are applicable to smaller reporting companies. A "smaller reporting company" is an issuer that is not an investment company or asset-backed issuer or majority-owned subsidiary and that (i) had a public float of less than $75 million as of the last business day of its most recently completed second fiscal quarter; or (ii) in the case of an initial registration statement, had a public float of less than $75 million as of a date within days of the filing of the registration statement; or (iii) in the case of an issuer whose public float as calculated by (i) or (ii) is zero, had annual revenues of less than $75 million during the most recently completed fiscal year for which audited financial statements are available.

**Annual Reports on Form 10-K**

All smaller reporting companies are required to file an annual report with the SEC on Form 10-K within 90 days of the end of its fiscal year. An extension of up to 15 calendar days is available for a Form 10-K as long as the extension notice on Form 12b-25 is filed no later than the next business day after the original filing deadline.

A Form 10-K includes the company's audited annual financial statements, a discussion of the company's business results, a summary of operations, a description of the overall business and its physical property, identification of any subsidiaries or affiliates, disclosure of the revenues contributed by major products or departments, and information on the number of shareholders, the management team and their salaries, and the interests of management and shareholders in certain transactions. A Form 10-K is substantially similar to a Form 10 registration statement and updates shareholders and the market on information previously filed in a registration statement, on an annual basis.

## Quarterly Reports on Form 10-Q

All smaller reporting companies are required to file a quarterly report on Form 10-Q within 45 days of the end of each of its fiscal quarters. An extension of up to 5 calendar days is available for a Form 10-Q as long as the extension notice on Form 12b-25 is filed no later than the next business day after the original filing deadline.

The quarterly report includes unaudited financial statements and information about the company's business and results for the previous three months and for the year to date. The quarterly report compares the company's performance in the current quarter and year to date to the same periods in the previous year.

## Current Reports on Form 8-K

Subject to certain exceptions, a Form 8-K must be filed within four (4) business days after the occurrence of the event being disclosed. No extension is available for an 8-K. Companies file this report with the SEC to announce major or extraordinary events that shareholders should know about, including entry into material agreements, mergers and acquisitions, change in control, changes in auditors, the issuance of unregistered securities, amendments in company articles or bylaws, company name changes, issues with reliance on previously issued financial statements, changes in officer or directors, bankruptcy proceedings, change in shell status regulation F-D disclosures and voluntary disclosures (voluntary disclosures have no filing deadline).

The Fair Disclosure Regulation, enacted in 2000 ("Regulation FD"), stipulates that publicly traded companies broadly and publicly disseminate information instead of distributing it selectively to certain analysts or investors only. Companies are encouraged to use several means of information dissemination including Form 8-K, news releases, Web sites or Web casts, and press releases. A Form 8-K under Regulation FD must be filed (i) simultaneously with the release of the material that is the subject of the filing (generally a press release); or (ii) the next trading day.

Other than when there has been a change of shell status, the financial statements of an acquired business must be filed no later than 71 calendar days after the date the initial Form 8-K was filed reporting the closing of the business acquisition (which initial Form 8-K is due with 4 days).

**Consequences and Issues Related to Late Filing**

Late filings carry severe consequences to small business issuers. Generally the shareholders of late filing issuers cannot rely on Rule 144 for the sale or transfer of securities while the issuer is delinquent in its filing requirements. Rule 144(c) requires that adequate current public information with respect to the company must be available. The current public information requirement is measured at the time of each sale of securities. That is, the issuer, whether reporting or non-reporting, must satisfy the current public information requirements as set forth in Rule 144(c) at the time that each resale of securities is made in reliance on Rule 144. For reporting issuers, adequate current public information is deemed available if the issuer is, and has been for a period of at least 90 days immediately before the sale, subject to the Exchange Act reporting requirements and has filed all required reports, other than Form 8-K, and has submitted electronically and posted on its website, if any, all XBRL data required to be submitted and posted.

An issuer that is late or has failed to maintain its reporting requirements is disqualified from use of Form S-3, which is needed to conduct at-the-market direct public offerings, shelf registrations and types of registered securities. Likewise, a Form S-8 cannot be filed while an issuer is either late or delinquent in its reporting requirements. Late or delinquent filings may also trigger a default in the terms of contracts, including corporate financing transactions. Finally, the SEC can bring enforcement proceedings against late filers, including actions to deregister the securities.

**Proxy Statements**

All companies with securities registered under the Exchange Act (i.e., through the filing of a Form 10 or Form 8-A) are subject to the Exchange Act proxy requirements found in Section 14 and the rules promulgated thereunder. Companies required to file reports as a result of an S-1 registration statement that have not separately registered under the Exchange Act are not subject to the proxy filing requirements. The proxy rules govern the disclosure in materials used to solicit shareholders' votes in annual or special meetings held for the approval of any corporate action requiring shareholder approval.

The information contained in proxy materials must be filed with the SEC in advance of any solicitation to ensure compliance with the disclosure rules.

Solicitations, whether by management or shareholder groups, must disclose all important facts concerning the issues on which shareholders are asked to vote. The disclosure information filed with the SEC and ultimately provided to the shareholders is enumerated in SEC Schedule 14A.

Where a shareholder vote is not being solicited, such as when a company has obtained shareholder approval through written consent in lieu of a meeting, a company may satisfy its Section 14 requirements by filing an information statement with the SEC and mailing such statement to its shareholders. In this case, the disclosure information filed with the SEC and mailed to shareholders is enumerated in SEC Schedule 14C. As with the proxy solicitation materials filed in Schedule 14A, a Schedule 14C Information Statement must be filed in advance of final mailing to the shareholder and is reviewed by the SEC to ensure that all important facts are disclosed. However, Schedule 14C does not solicit or request shareholder approval (or any other action, for that matter), but rather informs shareholders of an approval already obtained and corporate actions which are imminent.

In either case, a preliminary Schedule 14A or 14C is filed with the SEC, who then review and comment on the filing. Upon clearing comments, a definitive Schedule 14A or 14C is filed and mailed to the shareholders as of a certain record date.

Generally, the information requirements in Schedule 14C are less arduous than those in a Schedule 14A in that they do not include lengthy material regarding what a shareholder must do to vote or approve a matter. Moreover, the Schedule 14C process is much less time-consuming, as the shareholder approval has already been obtained. Accordingly, when possible, companies prefer to utilize the Schedule 14C Information Statement as opposed to the Schedule 14A Proxy Solicitation.

## Reporting Requirements for Company Insiders

All executive officers and directors and 10%-or-more shareholders of a company with securities registered under the Exchange Act (i.e., through the filing of a Form 10 or Form 8-A) are subject to the Exchange Act Reporting Requirements related to the reporting of certain transactions. The initial filing is on Form 3 and is due no later than ten days of becoming an officer, director, or beneficial owner. Changes in ownership are reported on Form 4 and must be reported to the SEC within two business days. Insiders must file a Form 5 to report any transactions that should have been reported earlier on a Form 4 or were eligible for deferred reporting. If a form must be filed, it is due 45 days after the end of the company's fiscal year. For more information on these Section 16 reporting requirements, see my blog Here.

## Additional Disclosures

Other federal securities laws and SEC rules require disclosures about a variety of events affecting the company. Under the Exchange Act, parties who will own more than five percent of a class of the company's securities after making a tender offer for securities registered under the Exchange Act must file a Schedule TO with the SEC. The SEC also requires any person acquiring more than five percent of a voting class of a company's Section 12 registered equity securities directly or by tender offer to file a Schedule 13D. Depending upon the facts and circumstances, the person or group of persons may be eligible to file the more abbreviated Schedule 13G in lieu of Schedule 13D. For more information on Schedules 13D/G, see my blog Here.

## Termination of Reporting Requirements

To deregister and suspend Reporting Requirements, an eligible issuer can file a Form 15. To qualify to file a Form 15, an issuer must either have (i) fewer than 300 shareholders; or (ii) fewer than 500 shareholders and the issuer's assets do not exceed $10 million.

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Securities Law Blog is written by Laura Anthony, Esq., a going public lawyer focused on OTC Listing Requirements, Direct Public Offerings, Going Public Transactions, Reverse Mergers, Form 10 Registration Statements, and Form S-1 Registration Statements. Securities Law Blog covers topics ranging from SEC Compliance, FINRA Compliance, DTC Chills, Going Public on the OTC, and OTCQX and OTCQB Reporting Requirements. Ms. Anthony is also the host of LawCast.com, the securities law network.

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