Updated SEC Guidance Will Require Many Public Companies to Revise their Presentation of Non-GAAP Information

New and Revised C&DIs Criticize Several Common Practices Relating to Non-GAAP Disclosures

On May 17, 2016, the Securities and Exchange Commission’s (SEC’s) Division of Corporation Finance (Division) published updated Compliance & Disclosure Interpretations (C&DIs) relating to the use of non-GAAP financial measures. These C&DIs represent a significant change in the Division’s approach to non-GAAP financial measures, which will also be reflected in how the Division reviews and comments on SEC filings. In advance of their next quarterly earnings releases, companies should evaluate their use and presentation of non-GAAP financial measures in view of the new and revised C&DIs, including disclosures about the reasons why management believes that presentation of the non-GAAP financial measures provides useful information to investors. Companies should expect an increase in SEC comment letters on non-GAAP financial measures as a result of these C&DIs. The full text of the updated C&DIs is available here, and the Appendix to this Sidley Update includes a comparison highlighting the C&DIs that were added or modified.

Background

Although non-GAAP financial measures have always been subject to Exchange Act Section 10(b) liability, the SEC’s regulation of these disclosures can be said to have started in January 2002, when the SEC brought its first enforcement case addressing the abuse of non-GAAP financial measures (then called pro forma earnings figures). The respondent was Trump Hotels & Casino Resorts, Inc., and the Commission found that Trump Hotels’ third quarter 1999 earnings release used pro forma earnings figures that excluded a one-time charge to tout the company’s purportedly positive results of operations but failed to disclose that those results were primarily attributable to a one-time gain rather than to improvements in operations.

Later in 2002, the Sarbanes-Oxley Act was enacted, Section 401 of which directed the SEC to adopt rules providing that pro forma financial information included in any SEC filing or in any public disclosure must be presented in a manner that does not contain any material misstatements or omissions and be reconciled with GAAP. Accordingly, the SEC adopted Regulation G and Item 10(e) of Regulation S-K. Regulation G generally applies to all public disclosures of material information that includes non-GAAP financial measures, whether or not the information is filed or furnished with the SEC. Item 10(e) of Regulation S-K generally applies to all SEC filings and earnings releases furnished under Item 2.02 of Form 8-K that include non-GAAP financial measures.
Regulation G and Item 10(e) of Regulation S-K also apply to foreign private issuers, subject to certain exceptions.

In recent years, the Division has encouraged companies using non-GAAP financial measures outside of their SEC filings, such as in presentations to investors and analysts, to include those measures in their SEC filings. The primary reason for this was the view that companies should communicate with investors in a consistent manner – the story told outside of a company’s SEC filings should be the same as the story in the company’s SEC filings. Moreover, if included in an SEC filing, the non-GAAP financial measure would be subject to the additional disclosure requirements in Item 10(e) as well as to the full panoply of liability provisions in the Exchange Act and, if incorporated by reference into a registration statement, the Securities Act.

Updates to C&DI

In this section we highlight the most significant of the updated C&DI.

**Presentation of GAAP Measures With Equal or Greater Prominence**

New C&DI Question 102.10 relates to the requirement in Item 10(e) of Regulation S-K, but not in Regulation G, that, whenever a non-GAAP financial measure is included in an SEC filing or an earnings release furnished under Item 2.02 of Form 8-K, the most directly comparable GAAP measure must be presented “with equal or greater prominence.” This C&DI marks the most dramatic shift in the Division’s approach to non-GAAP financial measures – from a permissive stance to a highly prescriptive one. In this C&DI, the Division provides examples of disclosures that it believes would cause a non-GAAP measure to be more “prominent” than its corresponding GAAP measure and therefore violate Item 10(e). A number of the examples are surprising because they label as improper several practices commonly used by public companies in the context of earnings releases. Certain material considerations relating to earnings releases in light of C&DI Question 102.10 are highlighted in the box below.

### Important Practical Implications for Earnings Releases

In C&DI Question 102.10, the Division identifies several practices that it believes improperly give greater prominence to non-GAAP measures than the corresponding GAAP measures. A number of the practices identified as problematic in the C&DI are common in public company earnings releases. Common earnings release practices that the Division has indicated are no longer acceptable include:

- **Having a non-GAAP measure precede its most directly comparable GAAP measure.** Companies must always list the GAAP measure first. It is not acceptable to have a non-GAAP measure precede its comparable GAAP measure.

- **Including only non-GAAP measures in a headline or caption.** It is not acceptable to include a non-GAAP measure in a headline unless the comparable GAAP measure is also included and such comparable GAAP measure precedes the non-GAAP measure.

- **Providing a qualitative description of performance on a non-GAAP basis without providing an equally prominent description of performance on a GAAP basis.** It would not be acceptable, for example, to explain that a company had “record performance” or “exceptional” performance on a non-GAAP basis without providing an equally prominent descriptive characterization of performance on a GAAP basis.

- **Including tabular disclosure of non-GAAP measures only.** If non-GAAP measures are included in a table, GAAP measures must also be included in the table or presented in their own, equally prominent table.
**Including forward-looking information on a non-GAAP basis only without explaining why it is not possible to present the forward-looking information on a GAAP basis.** Regulation G and Item 10(e) of Regulation S-K provide that a reconciliation is required for forward-looking information presented on a non-GAAP basis “to the extent available without unreasonable efforts.” Many companies have relied on this language to omit a reconciliation of forward-looking information. Companies that do this must now disclose that they are doing so and also identify the information that is unavailable and its probable significance in a location of equal or greater prominence.

**Providing a discussion and analysis of a non-GAAP measure without including a discussion and analysis of the most directly comparable GAAP measure.** Any time a company includes a discussion and analysis of a non-GAAP measure in an earnings release or other filing, it must also include an equally prominent discussion and analysis of the GAAP measure.

### Potentially Misleading Non-GAAP Measures

New C&DI Questions 100.01 through 100.04 relate to Regulation G’s and Item 10(e)’s requirement that non-GAAP measures not be misleading. In these C&DI’s, the Division states that, even when a particular non-GAAP measure includes an adjustment that is not explicitly prohibited and that is accurately and fully disclosed, the presentation of such non-GAAP measure can still be misleading. The Division provides examples of adjustments that it believes could lead to a misleading non-GAAP presentation, including:

- **An adjustment excluding normal, recurring, cash operating expenses necessary to operate a company’s business.** C&DI Question 100.01 indicates that, even though such an adjustment may not be explicitly prohibited, it could still be misleading.

- **An adjustment that is presented inconsistently between periods.** C&DI Question 100.02 indicates that such an adjustment could be misleading unless (1) the change in such adjustment between periods is disclosed, (2) the reasons for the change are explained and (3) if the change is sufficiently significant, the related non-GAAP presentation from prior periods is recast to conform to the current presentation.

- **An adjustment that excludes one-time charges without an adjustment that excludes one-time gains.** C&DI Question 100.03 indicates that it could be misleading to exclude non-recurring charges when non-recurring gains during the same period were not excluded. This was the basis for the SEC’s case against Trump Hotels.

- **An adjustment that substitutes individually tailored recognition and measurement methods for those required under GAAP.** C&DI Question 100.04 indicates that it could be misleading to use such an adjustment for revenue (such as accelerating the recognition of revenue to have revenue earned when customers are billed rather than earned ratably over time in accordance with GAAP) or other financial statement line items.

Public companies should review their non-GAAP measures carefully to determine if they include any adjustments of the type described above and consider what actions should be taken to prevent potentially misleading presentations. Although not expressly addressed by the updates, the updated C&DI’s would appear to suggest that foreign private issuers should also review their non-GAAP financial measures for potentially misleading presentations even where such measures would otherwise be permissible under the note to Item 10(e) of Regulation S-K as measures that are “expressly permitted” by the GAAP standard setter applicable to the foreign private issuer.
Presentation of Non-GAAP Measures on a Per Share Basis

The Division also updated C&DI Questions 102.02, 102.05, 102.07 and 103.02 to emphasize that a non-GAAP measure that can be used as a liquidity measure may not be presented on a per share basis. The Division noted that the determination of whether a measure is a liquidity measure depends on (1) the nature of the adjustments included in such measure (see C&DI Question 102.02) and (2) whether, based on the substance of such measure, such measure can be used as a liquidity measure, even if management characterizes such measure solely as a performance measure (see C&DI Question 102.05). In order to determine whether a particular per share presentation of a non-GAAP measure is acceptable, a public company should review such non-GAAP measure carefully to determine if it could potentially be used as a liquidity measure. CD&I Question 103.02 specifically states that EBIT and EBITDA, regardless of whether they are presented only as performance measures, must not be presented on a per share basis.

Presentation of FFO by REITs and Other Public Companies

The updates to C&DI Questions 102.01 and 102.02 continue to recognize that real estate investment trusts (REITs) and other public companies may present funds from operations (FFO) on a basis other than as defined by the National Association of Real Estate Investment Trusts (NAREIT), provided that any adjustments, among other things, comply with Item 10(e) of Regulation S-K and not violate Rule 100(b) of Regulation G. The updates, however, highlight the Division’s concern that adjustments to the NAREIT definition of FFO made by a REIT or other public company, depending upon their nature, may result in an adjusted measure that is a liquidity measure, for which per share information is prohibited. REITs and other public companies that present (or would like to present) an adjusted FFO measure on a per share basis should carefully review their FFO adjustments to determine whether such adjusted measure could potentially be used as a liquidity measure and, as a result, make such a per share presentation impermissible.

Calculation and Presentation of Income Tax Effects Related to Adjustments

In a substantially revised C&DI Question 102.11, the Division indicates that, for certain non-GAAP measures, income tax effects should be provided. For liquidity measures, the Division noted that an adjustment to GAAP taxes to show taxes paid in cash might be acceptable, and, for performance measures, the Division indicated that current and deferred income tax expense should be included. The Division further clarified that income taxes should be shown as a separate adjustment and clearly explained rather than simply indicating that an adjustment is “net of tax.” Public companies should review their non-GAAP measures carefully to determine whether their calculation or presentation of any adjustments related to income tax should be modified.

If you have any questions regarding this Sidley Update, please contact the Sidley lawyer with whom you usually work, or

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Comparison Highlighting Updates to C&DIs on Non-GAAP Financial Measures

Non-GAAP Financial Measures

Last Update: July 8, May 17, 2016
These Compliance & Disclosure Interpretations (C&DIs) comprise the Division’s interpretations of the rules and regulations on the use of non-GAAP financial measures. The bracketed date following each C&DI is the latest date of publication or revision.

QUESTIONS AND ANSWERS OF GENERAL APPLICABILITY

Section 100. General
Question 100.01

Question: Can certain adjustments, although not explicitly prohibited, result in a non-GAAP measure that is misleading?

Answer: Yes. Certain adjustments may violate Rule 100(b) of Regulation G because they cause the presentation of the non-GAAP measure to be misleading. For example, presenting a performance measure that excludes normal, recurring, cash operating expenses necessary to operate a registrant’s business could be misleading. [May 17, 2016]

Question 100.02

Question: Can a non-GAAP measure be misleading if it is presented inconsistently between periods?

Answer: Yes. For example, a non-GAAP measure that adjusts a particular charge or gain in the current period and for which other, similar charges or gains were not also adjusted in prior periods could violate Rule 100(b) of Regulation G unless the change between periods is disclosed and the reasons for it explained. In addition, depending on the significance of the change, it may be necessary to recast prior measures to conform to the current presentation and place the disclosure in the appropriate context. [May 17, 2016]

Question 100.03

Question: Can a non-GAAP measure be misleading if the measure excludes charges, but does not exclude any gains?

Answer: Yes. For example, a non-GAAP measure that is adjusted only for non-recurring charges when there were non-recurring gains that occurred during the same period could violate Rule 100(b) of Regulation G. [May 17, 2016]

Question 100.04

Question: A registrant presents a non-GAAP performance measure that is adjusted to accelerate revenue recognized ratably over time in accordance with GAAP as though it earned revenue when customers are billed. Can this measure be presented in documents filed or furnished with the Commission or provided elsewhere, such as on company websites?

Answer: No. Non-GAAP measures that substitute individually tailored revenue recognition and measurement methods for those of GAAP could violate Rule 100(b) of Regulation G. Other measures that use individually tailored recognition and measurement methods for financial statement line items other than revenue may also violate Rule 100(b) of Regulation G. [May 17, 2016]
Section 101. Business Combination Transactions

Question 101.01

**Question:** Does the exemption from Regulation G and Item 10(e) of Regulation S-K for non-GAAP financial measures disclosed in communications relating to a business combination transaction extend to the same non-GAAP financial measures disclosed in registration statements, proxy statements and tender offer materials?

**Answer:** No. There is an exemption from Regulation G and Item 10(e) of Regulation S-K for non-GAAP financial measures disclosed in communications subject to Securities Act Rule 425 and Exchange Act Rules 14a-12 and 14d-2(b)(2); it is also intended to apply to communications subject to Exchange Act Rule 14d-9(a)(2). This exemption does not extend beyond such communications. Consequently, if the same non-GAAP financial measure that was included in a communication filed under one of those rules is also disclosed in a Securities Act registration statement or a proxy statement or tender offer statement, no exemption from Regulation G and Item 10(e) of Regulation S-K would be available for that non-GAAP financial measure.

In addition, there is an exemption from Regulation G and Item 10(e) of Regulation S-K for non-GAAP financial measures disclosed pursuant to Item 1015 of Regulation M-A, which applies even if such non-GAAP financial measures are included in Securities Act registration statements, proxy statements and tender offer statements. [Jan. 11, 2010]

Question 101.02

**Question:** If reconciliation of a non-GAAP financial measure is required and the most directly comparable measure is a “pro forma” measure prepared and presented in accordance with Article 11 of Regulation S-X, may companies use that measure for reconciliation purposes, in lieu of a GAAP financial measure?

**Answer:** Yes. [Jan. 11, 2010]

Section 102. Item 10(e) of Regulation S-K

Question 102.01

**Question:** What measure was contemplated by “funds from operations” in footnote 50 to Exchange Act Release No. 47226, Conditions for Use of Non-GAAP Financial Measures, which indicates that companies may use “funds from operations per share” in earnings releases and materials that are filed or furnished to the Commission, subject to the requirements of Regulation G and Item 10(e) of Regulation S-K?

**Answer:** The reference to “funds from operations” in footnote 50, or “FFO,” refers to the measure as defined and clarified, as of January 1, 2000, by the National Association of Real Estate Investment Trusts (NAREIT). NAREIT has revised and clarified the definition since 2000. The staff accepts this NAREIT’s definition of FFO in effect as of May 17, 2016 as a performance measure and, as a performance measure, it may be presented does not object to its presentation on a per share basis. [Jan. 11, May 17, 2010, 2016]

Question 102.02

**Question:** May a registrant present “funds from operations” or “FFO” on a basis other than as defined and clarified, as of January 1, 2000, by the National Association of Real Estate Investment Trusts by NAREIT as of May 17, 2016?

**Answer:** Yes, provided that any adjustments made to “funds from operations” as defined in footnote 50 of Exchange Act Release No. 47226, FFO comply with Item 10(e) of Regulation S-K and the measure does not violate Rule 100(b) of Regulation G. Any adjustments made to “funds from operations” as defined in footnote 50, FFO must comply with the requirements of Item 10(e) of Regulation S-K for a performance measure or a liquidity measure, depending on how it is presented. If the adjusted measure is a performance measure, it may be presented the nature of the adjustments, some of which may trigger the prohibition on presenting this measure on a per share basis; if it is a liquidity measure, it may not be. [Jan. 11, 2010. See Section 100 and Question 102.05. [May 17, 2016]
Question 102.03

**Question:** Item 10(e) of Regulation S-K prohibits adjusting a non-GAAP financial performance measure to eliminate or smooth items identified as non-recurring, infrequent or unusual; when the nature of the charge or gain is such that it is reasonably likely to recur within two years or there was a similar charge or gain within the prior two years. Is this prohibition based on the description of the charge or gain, or is it based on the nature of the charge or gain?

**Answer:** The prohibition is based on the description of the charge or gain that is being adjusted. It would not be appropriate to state that a charge or gain is non-recurring, infrequent or unusual unless it meets the specified criteria. The fact that a registrant cannot describe a charge or gain as non-recurring, infrequent or unusual, however, does not mean that the registrant cannot adjust for that charge or gain. Registrants can make adjustments they believe are appropriate, subject to Regulation G and the other requirements of Item 10(e) of Regulation S-K. [Jan. 11, 2010] See Question 100.01. [May 17, 2016]

Question 102.04

**Question:** Is the registrant required to use the non-GAAP measure in managing its business or for other purposes in order to be able to disclose it?

**Answer:** No. Item 10(e)(1)(i)(D) of Regulation S-K states only that, “[t]o the extent material,” there should be a statement disclosing the additional purposes, “if any,” for which the registrant’s management uses the non-GAAP financial measure. There is no prohibition against disclosing a non-GAAP financial measure that is not used by management in managing its business. [Jan. 11, 2010]

Question 102.05

**Question:** While Item 10(e)(1)(ii) of Regulation S-K does not prohibit the use of per share non-GAAP financial measures, the adopting release for Item 10(e), Exchange Act Release No. 47226, states that “per share measures that are prohibited specifically under GAAP or Commission rules continue to be prohibited in materials filed with or furnished to the Commission.” In light of Commission guidance, specifically Accounting Series Release No. 142, Reporting Cash Flow and Other Related Data, and Accounting Standards Codification 230, are non-GAAP earnings per share numbers prohibited in documents filed or furnished with the Commission?

**Answer:** No. Item 10(e) recognizes that certain non-GAAP per share performance measures may be meaningful from an operating standpoint. Non-GAAP per share performance measures should be reconciled to GAAP earnings per share. On the other hand, non-GAAP liquidity measures, such as that measure cash flow, should be generated. Whether per share data is prohibited depends on whether the non-GAAP measure can be used as a liquidity measure, even if management presents it solely as a performance measure. When analyzing these questions, the staff will focus on the substance of the non-GAAP measure and not management’s characterization of the measure. [May 17, 2016]

Question 102.06

**Question:** Is Item 10(e)(1)(i) of Regulation S-K, which requires the prominent presentation of, and reconciliation to, the most directly comparable GAAP financial measure or measures, intended to change the staff’s practice of requiring the prominent presentation of amounts for the three major categories of the statement of cash flows when a non-GAAP liquidity measure is presented?

**Answer:** No. The requirements in Item 10(e)(1)(i) are consistent with the staff’s practice. The three major categories of the statement of cash flows should be presented when a non-GAAP liquidity measure is presented. [Jan. 11, 2010]

Question 102.07

**Question:** Some companies present a measure of “free cash flow,” which is typically calculated as cash flows from operating activities as presented in the statement of cash flows under GAAP, less capital expenditures. Does Item 10(e)(1)(ii) of Regulation S-K prohibit this measure in documents filed with the Commission?
Answer: No. The deduction of capital expenditures from the GAAP financial measure of cash flows from operating activities would not violate the prohibitions in Item 10(e)(1)(ii). However, companies should be aware that this measure does not have a uniform definition and its title does not describe how it is calculated. Accordingly, a clear description of how this measure is calculated, as well as the necessary reconciliation, should accompany the measure where it is used. Companies should also avoid inappropriate or potentially misleading inferences about its usefulness. For example, “free cash flow” should not be used in a manner that inappropriately implies that the measure represents the residual cash flow available for discretionary expenditures, since many companies have mandatory debt service requirements or other non-discretionary expenditures that are not deducted from the measure. [Jan. 11, 2010 Also, free cash flow is a liquidity measure that must not be presented on a per share basis. See Question 102.05. [May 17, 2016]

Question 102.08

Question: Does Item 10(e) of Regulation S-K apply to filed free writing prospectuses?

Answer: Regulation S-K applies to registration statements filed under the Securities Act, as well as registration statements, periodic and current reports and other documents filed under the Exchange Act. A free writing prospectus is not filed as part of the issuer’s registration statement, unless the issuer files it on Form 8-K or otherwise includes it or incorporates it by reference into the registration statement. Therefore, Item 10(e) of Regulation S-K does not apply to a filed free writing prospectus unless the free writing prospectus is included in or incorporated by reference into the issuer’s registration statement or included in an Exchange Act filing. [Jan. 11, 2010]

Question 102.09

Question: Item 10(e)(1)(ii)(A) of Regulation S-K prohibits “excluding charges or liabilities that required, or will require, cash settlement, or would have required cash settlement absent an ability to settle in another manner, from non-GAAP liquidity measures, other than the measures earnings before interest and taxes (EBIT) and earnings before interest, taxes, depreciation and amortization (EBITDA).” A company’s credit agreement contains a material covenant regarding the non-GAAP financial measure “Adjusted EBITDA.” If disclosed in a filing, the non-GAAP financial measure “Adjusted EBITDA” would violate Item 10(e), as it excludes charges that are required to be cash settled. May a company nonetheless disclose this non-GAAP financial measure?

Answer: Yes. The prohibition in Item 10(e) notwithstanding, because MD&A requires disclosure of material items affecting liquidity, if management believes that the credit agreement is a material agreement, that the covenant is a material term of the credit agreement and that information about the covenant is material to an investor’s understanding of the company’s financial condition and/or liquidity, then the company may be required to disclose the measure as calculated by the debt covenant as part of its MD&A. In disclosing the non-GAAP financial measure in this situation, a company should consider also disclosing the following:

- the material terms of the credit agreement including the covenant;
- the amount or limit required for compliance with the covenant; and
- the actual or reasonably likely effects of compliance or non-compliance with the covenant on the company’s financial condition and liquidity. [Jan. 11, 2010]

Question 102.10

Question: Item 10(e)(1)(i)(A) of Regulation S-K requires that when a registrant presents a non-GAAP measure it must present the most directly comparable GAAP measure with equal or greater prominence. This requirement applies to non-GAAP measures presented in documents filed with the Commission and also earnings releases furnished under Item 2.02 of Form 8-K. Are there examples of disclosures that would cause a non-GAAP measure to be more prominent?

Answer: Yes. Although whether a non-GAAP measure is more prominent than the comparable GAAP measure generally depends on the facts and circumstances in which the disclosure is made, the staff would consider the following examples of disclosure of non-GAAP measures as more prominent:
• Question: Is it appropriate to present a full non-GAAP income statement for purposes of reconciling non-GAAP measures to the most directly comparable GAAP measures?

• Omitting comparable GAAP measures from an earnings release headline or caption that includes non-GAAP measures;

• Presenting a non-GAAP measure using a style of presentation (e.g., bold, larger font) that emphasizes the non-GAAP measure over the comparable GAAP measure;

• A non-GAAP measure that precedes the most directly comparable GAAP measure (including in an earnings release headline or caption);

• Describing a non-GAAP measure as, for example, “record performance” or “exceptional” without at least an equally prominent descriptive characterization of the comparable GAAP measure;

• Providing tabular disclosure of non-GAAP financial measures without preceding it with an equally prominent tabular disclosure of the comparable GAAP measures or including the comparable GAAP measures in the same table;

• Excluding a quantitative reconciliation with respect to a forward-looking non-GAAP measure in reliance on the “unreasonable efforts” exception in Item 10(e)(1)(i)(B) without disclosing that fact and identifying the information that is unavailable and its probable significance in a location of equal or greater prominence; and

• Providing discussion and analysis of a non-GAAP measure without a similar discussion and analysis of the comparable GAAP measure in a location with equal or greater prominence. [May 17, 2016]

Answer: Generally, no. Presenting a full non-GAAP income statement may attach undue prominence to the non-GAAP information. [Jan. 11, 2010]

Question 102.11

Question: How should income tax effects related to adjustments to arrive at a non-GAAP measure be calculated and presented?

Question: May a registrant present an adjustment “net of tax” when reconciling a non-GAAP performance measure to the most directly comparable GAAP measure?

Answer: A registrant should provide income tax effects on its non-GAAP measures depending on the nature of the measures. If a measure is a liquidity measure that includes income taxes, it might be acceptable to adjust GAAP taxes to show taxes paid in cash. If a measure is a performance measure, the registrant should include current and deferred income tax expense commensurate with the non-GAAP measure of profitability. In addition, adjustments to arrive at a non-GAAP measure should not be presented “net of tax.” Rather, income taxes should be shown as a separate adjustment and clearly explained. [May 17, 2016]

Answer: Yes, provided that the tax effect of each reconciling item is disclosed parenthetically or in a footnote to the reconciliation. Alternatively, the company can present the tax effect in one line in the reconciliation. Regardless of the format of the presentation, registrants should disclose how the tax effect was calculated. [Jan. 11, 2010]

Question 102.12

Question: A registrant discloses a financial measure or information that is not in accordance with GAAP or calculated exclusively from amounts presented in accordance with GAAP. In some circumstances, this financial information may have been prepared in accordance with guidance published by a government, governmental authority or self-regulatory organization that is applicable to the registrant, although the information is not required disclosure by the government, governmental authority or self-regulatory organization. Is this information considered to be a “non-GAAP financial measure” for purposes of Regulation G and Item 10 of Regulation S-K?

Answer: Yes. Unless this information is required to be disclosed by a system of regulation that is applicable to the registrant, it is considered to be a “non-GAAP financial measure” under Regulation G and Item 10 of Regulation S-K. Registrants that disclose such information must provide the disclosures required by Regulation G or Item 10 of Regulation S-K, if applicable, including the quantitative reconciliation from the non-GAAP financial measure to the most comparable measure calculated in accordance with GAAP. This reconciliation should be in sufficient detail to allow a reader to understand the nature of the reconciling items. [Apr. 24, 2009]
Section 103. EBIT and EBITDA

Question 103.01

Question: Exchange Act Release No. 47226 describes EBIT as “earnings before interest and taxes” and EBITDA as “earnings before interest, taxes, depreciation and amortization.” What GAAP measure is intended by the term “earnings”? May measures other than those described in the release be characterized as “EBIT” or “EBITDA”? Does the exception for EBIT and EBITDA from the prohibition in Item 10(e)(1)(ii)(A) of Regulation S-K apply to these other measures?

Answer: “Earnings” means net income as presented in the statement of operations under GAAP. Measures that are calculated differently than those described as EBIT and EBITDA in Exchange Act Release No. 47226 should not be characterized as “EBIT” or “EBITDA” and their titles should be distinguished from “EBIT” or “EBITDA,” such as “Adjusted EBITDA.” These measures are not exempt from the prohibition in Item 10(e)(1)(ii)(A) of Regulation S-K, with the exception of measures addressed in Question 102.09. [Jan. 11, 2010]

Question 103.02

Question: If EBIT or EBITDA is presented as a performance measure, to which GAAP financial measure should it be reconciled?

Answer: If a company presents EBIT or EBITDA as a performance measure, such measures should be reconciled to net income as presented in the statement of operations under GAAP. Operating income would not be considered the most directly comparable GAAP financial measure because EBIT and EBITDA make adjustments for items that are not included in operating income. [Jan. 11, 2010] In addition, these measures must not be presented on a per share basis. See Question 102.05. [May 17, 2016]

Section 104. Segment Information

Question 104.01

Question: Is segment information that is presented in conformity with Accounting Standards Codification 280, pursuant to which a company may determine segment profitability on a basis that differs from the amounts in the consolidated financial statements determined in accordance with GAAP, considered to be a non-GAAP financial measure under Regulation G and Item 10(e) of Regulation S-K?

Answer: No. Non-GAAP financial measures do not include financial measures that are required to be disclosed by GAAP. Exchange Act Release No. 47226 lists “measures of profit or loss and total assets for each segment required to be disclosed in accordance with GAAP” as examples of such measures. The measure of segment profit or loss and segment total assets under Accounting Standards Codification 280 is the measure reported to the chief operating decision maker for purposes of making decisions about allocating resources to the segment and assessing its performance.

The list of examples in Exchange Act Release No. 47226 is not exclusive. As an additional example, because Accounting Standards Codification 280 requires or expressly permits the footnotes to the company's consolidated financial statements to include specific additional financial information for each segment, that information also would be excluded from the definition of non-GAAP financial measures. [Jan. 11, 2010]

Question 104.02

Question: Does Item 10(e)(1)(ii) of Regulation S-K prohibit the discussion in MD&A of segment information determined in conformity with Accounting Standards Codification 280?

Answer: No. Where a company includes in its MD&A a discussion of segment profitability determined consistent with Accounting Standards Codification 280, which also requires that a footnote to the company's consolidated financial statements provide a reconciliation, the company also should include in the segment discussion in the MD&A a complete discussion of the reconciling items that apply to the particular segment being discussed. In this regard, see Financial Reporting Codification Section 501.06.a, footnote 28. [Jan. 11, 2010]
Question 104.03

**Question:** Is a measure of segment profit/loss or liquidity that is not in conformity with Accounting Standards Codification 280 a non-GAAP financial measure under Regulation G and Item 10(e) of Regulation S-K?

**Answer:** Yes. Segment measures that are adjusted to include amounts excluded from, or to exclude amounts included in, the measure reported to the chief operating decision maker for purposes of making decisions about allocating resources to the segment and assessing its performance do not comply with Accounting Standards Codification 280. Such measures are, therefore, non-GAAP financial measures and subject to all of the provisions of Regulation G and Item 10(e) of Regulation S-K. [Jan. 11, 2010]

Question 104.04

**Question:** In the footnote that reconciles the segment measures to the consolidated financial statements, a company may total the profit or loss for the individual segments as part of the Accounting Standards Codification 280 required reconciliation. Would the presentation of the total segment profit or loss measure in any context other than the Accounting Standards Codification 280 required reconciliation in the footnote be the presentation of a non-GAAP financial measure?

**Answer:** Yes. The presentation of the total segment profit or loss measure in any context other than the Accounting Standards Codification 280 required reconciliation in the footnote would be the presentation of a non-GAAP financial measure because it has no authoritative meaning outside of the Accounting Standards Codification 280 required reconciliation in the footnotes to the company's consolidated financial statements. [Jan. 11, 2010]

Question 104.05

**Question:** Company X presents a table illustrating a breakdown of revenues by certain products, but does not sum this to the revenue amount presented on Company X's financial statements. Is the information in the table considered a non-GAAP financial measure under Regulation G and Item 10(e) of Regulation S-K?

**Answer:** No, assuming the product revenue amounts are calculated in accordance with GAAP. The presentation would be considered a non-GAAP financial measure, however, if the revenue amounts are adjusted in any manner. [Jan. 11, 2010]

Question 104.06

**Question:** Company X has operations in various foreign countries where the local currency is used to prepare the financial statements which are translated into the reporting currency under the applicable accounting standards. In preparing its MD&A, Company X will explain the reasons for changes in various financial statement captions. A portion of these changes will be attributable to changes in exchange rates between periods used for translation. Company X wants to isolate the effect of exchange rate differences and will present financial information in a constant currency — e.g., assume a constant exchange rate between periods for translation. Would such a presentation be considered a non-GAAP measure under Regulation G and Item 10(e) of Regulation S-K?

**Answer:** Yes. Company X may comply with the reconciliation requirements of Regulation G and Item 10(e) by presenting the historical amounts and the amounts in constant currency and describing the process for calculating the constant currency amounts and the basis of presentation. [Jan. 11, 2010]

**Section 105. Item 2.02 of Form 8-K**

**Question** 105.01

**Question:** Item 2.02 of Form 8-K contains a conditional exemption from its requirement to furnish a Form 8-K where earnings information is presented orally, telephonically, by webcast, by broadcast or by similar means. Among other conditions, the company must provide on its web site any financial and other statistical information contained in the presentation, together with any information that would be required by Regulation G. Would an audio file of the initial webcast satisfy this condition to the exemption?
**Answer:** Yes, provided that: (1) the audio file contains all material financial and other statistical information included in the presentation that was not previously disclosed, and (2) investors can access it and replay it through the company’s web site. Alternatively, slides or a similar presentation posted on the web site at the time of the presentation containing the required, previously undisclosed, material financial and other statistical information would satisfy the condition. In each case, the company must provide all previously undisclosed material financial and other statistical information, including information provided in connection with any questions and answers. Regulation FD also may impose disclosure requirements in these circumstances. [Jan. 11, 2010]

**Question 105.02**

**Question:** Item 2.02 of Form 8-K contains a conditional exemption from its requirement to furnish a Form 8-K where earnings information is presented orally, telephonically, by webcast, by broadcast or by similar means. Among other conditions, the company must provide on its web site any material financial and other statistical information not previously disclosed and contained in the presentation, together with any information that would be required by Regulation G. When must all of this information appear on the company's web site?

**Answer:** The required information must appear on the company’s web site at the time the oral presentation is made. In the case of information that is not provided in a presentation itself but, rather, is disclosed unexpectedly in connection with the question and answer session that was part of that oral presentation, the information must be posted on the company’s web site promptly after it is disclosed. Any requirements of Regulation FD also must be satisfied. A webcast of the oral presentation would be sufficient to meet this requirement. [Jan. 11, 2010]

**Question 105.03**

**Question:** Does a company’s failure to furnish to the Commission the Form 8-K required by Item 2.02 in a timely manner affect the company’s eligibility to use Form S-3?

**Answer:** No. Form S-3 requires the company to have filed in “a timely manner all reports required to be filed in twelve calendar months and any portion of a month immediately preceding the filing of the registration statement.” Because an Item 2.02 Form 8-K is furnished to the Commission, rather than filed with the Commission, failure to furnish such a Form 8-K in a timely manner would not affect a company’s eligibility to use Form S-3. While not affecting a company’s Form S-3 eligibility, failure to comply with Item 2.02 of Form 8-K would, of course, be a violation of Section 13(a) of the Exchange Act and the rules thereunder. [Jan. 11, 2010]

**Question 105.04** [withdrawn]

**Question 105.05**

**Question:** Company X files its quarterly earnings release as an exhibit to its Form 10-Q on Wednesday morning, prior to holding its earnings conference call Wednesday afternoon. Assuming that all of the other conditions of Item 2.02(b) are met, may the company rely on the exemption for its conference call even if it does not also furnish the earnings release in an Item 2.02 Form 8-K?

**Answer:** Yes. Company X’s filing of the earnings release as an exhibit to its Form 10-Q, rather than in an Item 2.02 Form 8-K, before the conference call takes place, would not preclude reliance on the exemption for the conference call. [Jan. 11, 2010]

**Question 105.06**

**Question:** Company A issues a press release announcing its results of operations for a just-completed fiscal quarter, including its expected adjusted earnings (a non-GAAP financial measure) for the fiscal period. Would this press release be subject to Item 2.02 of Form 8-K?

**Answer:** Yes, because it contains material, non-public information regarding its results of operations for a completed fiscal period. The adjusted earnings range presented would be subject to the requirements of Item 2.02 applicable to non-GAAP financial measures. [Jan. 11, 2010]
Question 105.07

**Question:** A company issues its earnings release after the close of the market and holds a properly noticed conference call to discuss its earnings two hours later. That conference call contains material, previously undisclosed, information of the type described under Item 2.02 of Form 8-K. Because of this timing, the company is unable to furnish its earnings release on a Form 8-K before its conference call. Accordingly, the company cannot rely on the exemption from the requirement to furnish the information in the conference call on a Form 8-K. What must the company file with regard to its conference call?

**Answer:** The company must furnish the material, previously non-public, financial and other statistical information required to be furnished on Item 2.02 of Form 8-K as an exhibit to a Form 8-K and satisfy the other requirements of Item 2.02 of Form 8-K. A transcript of the portion of the conference call or slides or a similar presentation including such information will satisfy this requirement. In each case, all material, previously undisclosed, financial and other statistical information, including that provided in connection with any questions and answers, must be provided. [Jan. 15, 2010]

**Section 106. Foreign Private Issuers**

Question 106.01

**Question:** The Note to Item 10(e) of Regulation S-K permits a foreign private issuer to include in its filings a non-GAAP financial measure that otherwise would be prohibited by Item 10(e)(1)(ii) if, among other things, the non-GAAP financial measure is required or expressly permitted by the standard setter that is responsible for establishing the GAAP used in the company’s primary financial statements included in its filing with the Commission. What does “expressly permitted” mean?

**Answer:** A measure is “expressly permitted” if the particular measure is clearly and specifically identified as an acceptable measure by the standard setter that is responsible for establishing the GAAP used in the company’s primary financial statements included in its filing with the Commission.

The concept of “expressly permitted” can be also be demonstrated with explicit acceptance of a presentation by the primary securities regulator in the foreign private issuer’s home country jurisdiction or market. Explicit acceptance by the regulator would include (1) published views of the regulator or members of the regulator’s staff or (2) a letter from the regulator or its staff to the foreign private issuer indicating the acceptance of the presentation — which would be provided to the Commission’s staff upon request. [Jan. 11, 2010]

Question 106.02

**Question:** A foreign private issuer furnishes a press release on Form 6-K that includes a section with non-GAAP financial measures. Can a foreign private issuer incorporate by reference into a Securities Act registration statement only those portions of the furnished press release that do not include the non-GAAP financial measures?

**Answer:** Yes. Reports on Form 6-K are not incorporated by reference automatically into Securities Act registration statements. In order to incorporate a Form 6-K into a Securities Act registration statement, a foreign private issuer must specifically provide for such incorporation by reference in the registration statement and in any subsequently submitted Form 6-K. See Item 6(c) of Form F-3. Where a foreign private issuer wishes to incorporate by reference a portion or portions of the press release provided on a Form 6-K, the foreign private issuer should either: (1) specify in the Form 6-K those portions of the press release to be incorporated by reference, or (2) furnish two Form 6-K reports, one that contains the full press release and another that contains the portions that would be incorporated by reference (and specifies that the second Form 6-K is so incorporated). Using a separate report on Form 6-K containing the portions that would be incorporated by reference may provide more clarity for investors in most circumstances. A company must also consider whether its disclosure is rendered misleading if it incorporates only a portion (or portions) of a press release. [Jan. 11, 2010]

Question 106.03

**Question:** A foreign private issuer publishes a non-GAAP financial measure that does not comply with Regulation G, in reliance on Rule 100(c), and then furnishes the information in a report on Form 6-K. Must the foreign private
issuer comply with Item 10(e) of Regulation S-K with respect to that information if the company chooses to incorporate that Form 6-K report into a filed Securities Act registration statement (other than an MJDS registration statement)?

**Answer:** Yes, the company must comply with all of the provisions of Item 10(e) of Regulation S-K. [Jan. 11, 2010]

**Question 106.04**

**Question:** If a Canadian company includes a non-GAAP financial measure in an annual report on Form 40-F, does the company need to comply with Regulation G or Item 10(e) of Regulation S-K with respect to that information if the company files a non-MJDS Securities Act registration statement that incorporates by reference the Form 40-F?

**Answer:** No. Information included in a Form 40-F is not subject to Regulation G or Item 10(e) of Regulation S-K. [Jan. 11, 2010]

**Section 107. Voluntary Filers**

**Question 107.01**

**Question:** Section 15(d) of the Exchange Act suspends automatically its application to any company that would be subject to the filing requirements of that section where, if other conditions are met, on the first day of the company’s fiscal year it has fewer than 300 holders of record of the class of securities that created the Section 15(d) obligation. This suspension, which relates to the fiscal year in which the fewer than 300 record holders determination is made on the first day thereof, is automatic and does not require any filing with the Commission. The Commission adopted Rule 15d-6 under the Exchange Act to require the filing of a Form 15 as a notice of the suspension of a company’s reporting obligation under Section 15(d). Such a filing, however, is not a condition to the suspension. A number of companies whose Section 15(d) reporting obligation is suspended automatically by the statute choose not to file the notice required by Rule 15d-6 and continue to file Exchange Act reports as though they continue to be required. Must a company whose reporting obligation is suspended automatically by Section 15(d) but continues to file periodic reports comply with Regulation G and the requirements of Item 10(e) of Regulation S-K?

**Answer:** Yes. Regulation S-K relates to filings with the Commission. Accordingly, a company that is making filings as described in this question must comply with Regulation S-K or Form 20-F, as applicable, in its filings.

As to other public communications, any company “that has a class of securities registered under Section 12 of the Securities Exchange Act of 1934, or is required to file reports under Section 15(d) of the Securities Exchange Act of 1934” must comply with Regulation G. The application of this standard to those companies that no longer are “required” to report under Section 15(d) but choose to continue to report presents a difficult dilemma, as those companies technically are not subject to Regulation G but their continued filing is intended to and does give the appearance that they are a public company whose disclosure is subject to the Commission’s regulations. It is reasonable that this appearance would cause shareholders and other market participants to expect and rely on a company’s required compliance with the requirements of the federal securities laws applicable to companies reporting under Section 15(d). Accordingly, while Regulation G technically does not apply to a company such as the one described in this question, the failure of such a company to comply with all requirements (including Regulation G) applicable to a Section 15(d)-reporting company can raise significant issues regarding that company’s compliance with the anti-fraud provisions of the federal securities laws. [Jan. 11, 2010]

**Section 108. Compensation Discussion and Analysis/Proxy Statement**

**Question 108.01**

**Question:** Instruction 5 to Item 402(b) provides that “[d]isclosure of target levels that are non-GAAP financial measures will not be subject to Regulation G and Item 10(e); however, disclosure must be provided as to how the number is calculated from the registrant’s audited financial statements.” Does this instruction extend to non-GAAP financial information that does not relate to the disclosure of target levels, but is nevertheless included in Compensation Discussion & Analysis (“CD&A”) or other parts of the proxy statement - for example, to explain the relationship between pay and performance?
**Answer:** No. Instruction 5 to Item 402(b) is limited to CD&A disclosure of target levels that are non-GAAP financial measures. If non-GAAP financial measures are presented in CD&A or in any other part of the proxy statement for any other purpose, such as to explain the relationship between pay and performance or to justify certain levels or amounts of pay, then those non-GAAP financial measures are subject to the requirements of Regulation G and Item 10(e) of Regulation S-K.

In these pay-related circumstances only, the staff will not object if a registrant includes the required GAAP reconciliation and other information in an annex to the proxy statement, provided the registrant includes a prominent cross-reference to such annex. Or, if the non-GAAP financial measures are the same as those included in the Form 10-K that is incorporating by reference the proxy statement’s Item 402 disclosure as part of its Part III information, the staff will not object if the registrant complies with Regulation G and Item 10(e) by providing a prominent cross-reference to the pages in the Form 10-K containing the required GAAP reconciliation and other information. [July 8, 2011]