

An IOSCO Technical Committee Release:

Cautionary Statement Regarding Non-GAAP Results Measures

19 May, 2002

The Technical Committee of the International Organization of Securities Commissions today issued the following Alert to issuer companies, investors and other users of financial information:

It has become common practice for many issuers to publish company-specific measurements of earnings other than those prescribed by Generally Accepted Accounting Principles (GAAP). Such "non-GAAP earnings measures" are commonly included in company press releases, but may also be included in periodic reports to shareholders and other information filed with securities regulators and stock exchanges.

Most non-GAAP earnings measures are derived from a company's net income determined in accordance with GAAP, or from some other intermediate total in the profit and loss statement, but with adjustments to include or exclude certain items. Certain elements of expenses may be excluded or reclassified, in which case the non-GAAP measures may present a more favorable picture of a company's earnings than does income measured according to GAAP.

Non-GAAP measures may be identified by terms such as "operating earnings", "cash earnings", "earnings before one-time charges", "EBITDA - earnings before interest, taxes, depreciation, and amortization", "adjusted earnings" and similar terms denoting adjustments to net income. Such non-GAAP earnings measures are also sometimes identified as "pro forma net income" or otherwise qualified with the use of the term "pro forma". (The term "pro forma" also has other applications in some countries' GAAP that do not relate to non-GAAP earnings measures, as in the case where pro forma comparisons are required by GAAP to show the effects of certain business combinations or accounting changes.)

Issuer companies using non-GAAP earnings measures may appropriately wish to provide investors with additional information that will focus on critical components of financial results in order to provide a meaningful comparison of period-to-period results. Properly used and presented, non-GAAP earnings measures can assist

investors in gaining a better understanding of a company's financial performance. A problem arises, however, if non-GAAP earnings measures are used inconsistently or are inadequately defined by a company, or if such measures are used in such a way as to obscure the financial results determined according to GAAP or provide an incomplete description of true financial results. Because non-GAAP financial information by its very nature departs from traditional accounting conventions, its use can make it hard for investors to compare an issuer's financial information with other reporting periods and with other companies. Improper use of non-GAAP earnings measures can mislead investors regarding a company's financial performance. Similarly, some issuers may publish non-GAAP information relating to the company's financial position, such as netting assets against indebtedness, which also could mislead investors regarding a company's true financial situation.

Issuers, investors and other users of financial information are cautioned to use care when presenting and interpreting non-GAAP results measures.

Among IOSCO member jurisdictions, statements of expectations or statements of cautionary advice regarding the proper use of non-GAAP information by issuers have been issued in a number of countries. Some examples of communications which have been issued include:

- A regulator's expectation that issuers will present prominently with the non-GAAP earnings measures the earnings measures for the period determined in accordance with GAAP, and provide a clear reconciliation between the two.
- A regulator's statement that whenever financial performance indicators of a non-GAAP nature are published in press releases or speeches, etc., they should always be accompanied by the indication of the net consolidated income/loss figure for the same period calculated in accordance with GAAP.
- A regulator's cautionary advice warning public companies that the antifraud provisions of national securities laws apply to the use of pro forma information, and further noting and commending private sector efforts that provide recommended guidelines for information in earnings press releases, such as the guidelines developed by Financial Executives International and the National Investor Relations Institute, and encouraging public companies to consider and follow those private sector recommendations. (The recommendations call for pro forma information to always be accompanied by a clearly described reconciliation to GAAP results.)

IOSCO recognizes that differences in legal requirements and reporting frequency in member jurisdictions may affect the specific practices and availability of GAAP information in each area, and reminds issuers of the responsibility in all instances to ensure that the information they provide to the public is not misleading. Selective editing of financial information may be misleading if it results in the omission of material information. Issuers are cautioned that regulatory actions may be taken if information is disclosed in a manner considered misleading.

Investors are encouraged to compare any summaries including non-GAAP earnings measures and pro-forma financial information with the official results reported on GAAP-based financials by the same company. Investors should be aware that non-GAAP pro-forma earnings measures are not prepared in accordance with the accounting standards applied to financial statements and may omit or reclassify significant expenses.

For further information, contact the IOSCO Secretary General, Mr. Philippe Richard, at 34 91 417 5549, or by E-mail: mail@oicv.iosco.org

Endnotes:

1. Generally Accepted Accounting Principles as used in this statement include both the national accounting standards of a country or jurisdiction and any other national or international accounting standards that are accepted by that jurisdiction for the financial statements of listed public companies.