



SEC STAFF UPDATES GUIDANCE ON USE OF NON-GAAP FINANCIAL MEASURES

On January 11 and 15, 2010, the SEC's Division of Corporate Finance issued new Compliance and Disclosure Interpretations (C&DIs) on the use of non-GAAP financial measures in SEC filings and other public disclosures that update and replace the SEC's previous guidance contained in the 2003 publication, *Regarding the Use of Non-GAAP Financial Measures—Frequently Asked Questions* (FAQs). The new C&DIs are intended to encourage companies to disclose more non-GAAP financial measures in their SEC filings. In recent public statements, the SEC has expressed concern that its 2003 FAQs may have discouraged companies from providing non-GAAP financial measures in their SEC filings. While much of the guidance from the 2003 FAQs is retained, the new C&DIs modify several of the SEC's previous interpretations, as well as add several new interpretations. This e-zine briefly discusses some of the more significant changes to the SEC's guidance on the use of non-GAAP financial measures but does not address every aspect of the new C&DIs. For a copy of the full text of the new C&DIs, [click here](#).

Recurring Items

Item 10(e) of Regulation S-K states that non-GAAP performance measures may not be adjusted to eliminate or smooth items identified as "nonrecurring, infrequent or unusual," when (i) the nature of the charge or gain is such that it is reasonably likely to recur within two years or (ii) there was a similar charge or gain within the prior two years. New C&DI 102.03 clarifies that the prohibition on adjusting a non-GAAP financial measure is based on the description, rather than the nature, of the charge or gain being adjusted. Thus, as long as a registrant does not incorrectly describe an adjustment as nonrecurring, infrequent or unusual, a non-GAAP financial measure may exclude recurring items.

Use by Management

C&DI 102.04 addresses whether disclosure of non-GAAP financial measures is limited only to those non-GAAP measures used in managing a registrant's business or for other purposes. Under Item 10(e) of Regulation S-K, a registrant is required to disclose why management believes a non-GAAP financial measure provides useful information and how management uses the non-GAAP financial measure. Noting Item 10(e)(1)(i)(D) of Regulation S-K is limited to disclosure "to the extent material" of management's additional uses of the non-GAAP measure, "if any," C&DI 102.04 makes clear that there is no prohibition on disclosure of non-GAAP financial measures in an SEC filing that management believes would be useful to investors, even if management does not use the non-GAAP financial measure to manage the registrant's business or for any other purposes.

Other Changes

- C&DI 102.05 confirms that registrants can disclose certain non-GAAP per-share performance measures, but cannot disclose non-GAAP per share liquidity measures.



- C&DI 102.08 clarifies that Item 10(e) of Regulation S-K generally does not apply to a filed free writing prospectus unless the issuer files it on a Form 8-K or otherwise includes it or incorporates it by reference into the registration statement. However, free writing prospectuses remain subject to Regulation G.
- C&DI 102.10 expresses the SEC's view that it is generally inappropriate to present a full non-GAAP income statement for purposes of reconciling non-GAAP measures to the most directly comparable GAAP measures.
- C&DI 102.11 clarifies that a registrant may present an adjustment "net of tax" when reconciling a non-GAAP performance measure to the most directly comparable GAAP measure provided (i) the tax effect of each reconciling item is disclosed parenthetically or in a footnote to the reconciliation, or (ii) the tax effect is presented in one line in the reconciliation.

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Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues, contact:

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