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FMA
FINANCIAL MARKETS AUTHORITY
TE MANA TATAI HOKOHOKO · NEW ZEALAND

Disclosing non-GAAP financial information

We describe financial information outside of financial statements that is not prepared and presented in accordance with generally accepted accounting practice (GAAP), or is presented as an alternative to statutory profit, as 'non-GAAP financial information.'

This guidance replaces our 2012 Guidance note: Disclosing non-GAAP financial information to reflect the requirements of the Financial Markets Conduct Act 2013 (FMC Act) and our findings from the review of non-GAAP financial information since 2012.

About this guidance note:

This guidance note is primarily for FMC reporting entities and their directors.

It aims to outline the FMA's expectations on the use of non-GAAP financial information.

Document history

This version was issued in July 2017 and is based on legislation and regulations as at the date of issue. It replaces the original version issued in September 2012.

FMA document reference code 3304784

Introduction

About this guidance note

This guidance note sets out our expectations on the use of financial information outside of the financial statements, where that information is not prepared and presented in accordance with generally accepted accounting practice (GAAP)[1], or is presented as an alternative to statutory profit. We describe this as 'non-GAAP financial information.'

It is primarily intended for Financial Markets Conduct Act reporting entities (FMC reporting entities) and their directors. However, we also encourage other entities to apply these principles when presenting non-GAAP financial information.

Every FMC reporting entity must comply with all regulatory requirements. We do not repeat all regulatory requirements in this guidance note but we refer to some, where appropriate. This guidance note does not replace GAAP or the law. Where a principle outlined in this guidance note is provided for, or contradicts with applicable regulatory requirements, regulatory requirements prevail[2].

This guidance note does not constitute legal advice. We encourage you to seek your own tailored professional advice.

Purpose

Non-GAAP financial information can be useful for FMC reporting entities, investors and others, as it can provide additional insight into an FMC reporting entity's financial performance, financial condition and/or cash flow.

However, it has the potential to be misleading if inconsistently presented, inadequately defined, not reconciled to the most comparable GAAP financial information and/or used to obscure financial results determined in accordance with GAAP.

This guidance note contains general principles that FMC reporting entities should follow when presenting non-GAAP financial information. Entities following these principles will contribute to the reliability and comparability over time of non-GAAP financial information and reduce the potential for misleading disclosure.

The purpose of this guidance is to:

- promote meaningful and transparent communication of financial information to investors and other users of non-GAAP financial information;
- help FMC reporting entities disclose financial information in a way that is not misleading; and
- increase market certainty about our views on disclosure of non-GAAP financial information and how we will assess such disclosures.

[1] Currently GAAP for the majority of FMC reporting entities in New Zealand is New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) which is based on International Financial Reporting Standards (IFRS).
Some FMC reporting entities may be Public Benefit Entities (PBEs), and for these entities the applicable GAAP is PBE Standards issued by External Reporting Board (XRB).

[2] For example, where the Financial Markets Conduct Regulations 2014 allow the substitution of GAAP financial information with pro-forma financial information in a Product Disclosure Statement, the principle on prominence will not apply by default.

Scope

This guidance note applies to any non-GAAP financial information an FMC reporting entity discloses outside the financial statements, including any non-GAAP financial information presented on a pro-forma basis.[3]

Non-GAAP financial information is commonly presented in:

- market announcements
- management commentary
- investor presentations
- disclosure documents filed with the Registrar and licenced market operators
- and other communications to shareholders and market participants.

Given the specific nature of pro-forma financial information, we have included a separate section at the end of this guidance note titled 'Disclosing pro-forma financial information' that provides additional specific principles and guidance on its preparation and presentation.

This guidance note also applies to any non-GAAP financial measures and non-GAAP profit measures added to and/or substituted for the selected financial information in a product disclosure statement (PDS) prescribed by the Financial Markets Conduct Regulations 2014 (FMC Regulations). This includes any pro-forma financial information added to or substituted for the selected financial information in the PDS.

Our work on non-GAAP financial information

In 2012 we released our guidance note on disclosing non-GAAP financial information (2012 guidance note).[4]

Since then we have continued to monitor how entities present non-GAAP financial information, including whether they have applied the principles and made supporting disclosures consistent with our expectations.

This guidance note updates and replaces the 2012 guidance note to reflect:

- the requirements under the FMC Act; and
- our observations and findings from the review of non-GAAP financial information since 2012.[5]

In June 2016, the International Organisation of Securities Commissions (IOSCO) released a statement on non-GAAP financial measures.[6] The FMA is a member of IOSCO and contributed to this statement. For the purposes of this guidance note, we have also aligned our position with the principles in the IOSCO statement except where those principle(s) were inappropriate (or inadequate) for the New Zealand market.

We have updated the principles outlined in 2012 guidance note as follows:

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[3] Pro-forma financial information is non-GAAP financial information that is intended to show the effects of proposed, completed or hypothetical events or transactions on the entity's financial position, performance, cash flows and/or prospects for illustrative purposes.

[4] http://fma.govt.nz/assets/Guidance/_versions/3406/120901-guidance-note-disclosing-non-gaap-financial-information.1.pdf

[5] In 2013 we released a monitoring report on how issuers had adopted the principals in our 2012 guidance note and suggested areas for improvement. The report can be found at https://fma.govt.nz/assets/Reports/130930-Monitoring-of-non-gaap-disclosures-2013.pdf

[6] IOSCO statement https://www.iosco.org/library/pubdocs/pdf/IOSCOPD532.pdf

- **Prominence:** we have updated this principle stating that non-GAAP financial information should not be presented with undue and *greater* prominence than the most comparable GAAP financial information. Our review of non-GAAP disclosures against the 2012 guidance note revealed entities often give greater prominence to non-GAAP financial information.

  In many cases, this resulted in an unbalanced view of their performance. By ensuring non-GAAP financial information is not given greater prominence, emphasis or authority, an entity is more likely to disclose information that presents a balanced 'whole' picture of its performance.

- **Reconciliation:** we have removed the proposal for a reconciliation to be provided in every document where non-GAAP financial information is disclosed. Instead, entities may provide a reference to where the reconciliation can be easily accessed.

- **One-off / non-recurring items:** we have updated this principle to specify that the policy to exclude one-off / non-recurring items should entail *all* items of such nature, regardless of whether they are related. This avoids cherry-picking of the adjustments and ensures the non-GAAP financial information reflects the entity's approach in its entirety.

We will assess all non-GAAP financial information disclosures against the principles in this guidance note from the date of publication.

Presenting non-GAAP financial information

Financial statements' primary purpose is to provide existing and potential investors, lenders and other creditors ('primary users' or 'users') with useful information to help them make informed decisions about the FMC reporting entity.

They also help primary users to assess management's stewardship of the resources entrusted to them. In other words, financial statements prepared in accordance with GAAP provide users with a defined basis for conducting financial analysis and aim to ensure comparison over time and amongst different entities.

For example, reporting of GAAP profit provides a reader with financial information that is consistently calculated and comparable over time and across all FMC reporting entities.

FMC reporting entities commonly supplement their GAAP based financial information with non-GAAP financial information they believe more accurately reflects their performance, financial position and/or cash flows.

Non-GAAP profit measures (also known as alternative performance measures), are one of the most common forms of non-GAAP financial information. Common terms include; 'underlying earnings', 'normalised profit', 'cash earnings', 'adjusted earnings' and 'earnings before non-recurring items'. These terms typically lack a standardised meaning and are generally not comparable between entities because they may use the same term to refer to different calculations.

In our view, additional disclosures should be made to reduce the risk of misleading disclosure when non-GAAP financial information is used.

The FMC Act contains a number of provisions that deal with misleading information including prohibiting:

- misleading or deceptive conduct (sections 19-21 of Part 2);
- the making of false or misleading representations (section 22 of Part 2);
- the making of unsubstantiated representations (section 23 of Part 2); and
- offers of financial products where there is:
  - a statement in the PDS, any accompanying application form or the register entry that is false or misleading or is likely to mislead;
  - an omission from the PDS, or the register entry, of information required to be contained in the PDS or the register entry; or
  - a circumstance that has arisen since the PDS was lodged with the Registrar that would have been required to be disclosed if it had arisen before the PDS was lodged, and the circumstance is not so disclosed or otherwise contained in the PDS or the register entry; and

  the matter is materially adverse from the point of view of an investor (section 82 of Part 3).

In the table below, we set out the principles on presenting non-GAAP financial information.

When disclosing non-GAAP financial information, management should exercise judgement when deciding how much information is needed to explain a particular measure. They should take into account how familiar their investors are with the measure, and the nature of the communication it is included in.

We encourage FMC reporting entities to have an internal policy, authorised by their directors, on the use and disclosure of non-GAAP financial information. This should be specific to the entity and consistently applied from period to period.

In addition to this guidance note, the 'Disclosure of non-GAAP financial information questions and answers' section on the FMA's website provides additional insight into specific aspects of the guidance note.

Guidance on presenting non-GAAP financial information

Principle	Explanation
Defining the non-GAAP financial information	*Definition* Entities should define non-GAAP financial information and support it with a clear explanation of the basis of calculation. *Clear labeling* Entities should clearly label non-GAAP financial information in a way that distinguishes it from GAAP financial information. The term or label should accurately describe and reflect the non-GAAP financial information. For example, it is not appropriate to label a measure as EBITDA if it excludes items which are not interest, tax, depreciation or amortisation. The term or label should not cause confusion with GAAP information. *Use of non-GAAP financial information* Entities should clearly explain the reasons for presenting the non-GAAP financial information, including: • why the information is useful to investors • how it is used internally by management[7]. Entities should make a statement that the non-GAAP financial information does not have a standardised meaning prescribed by GAAP and therefore may not be comparable to similar financial information presented by other entities. You should also disclose whether the non-GAAP financial information has been subject to audit or review[8].
Prominence	• Entities should not present non-GAAP financial information with undue and greater prominence, emphasis or authority than the most directly comparable GAAP financial information. • When presenting non-GAAP financial information, entities should not in any way confuse or obscure presentation of GAAP financial information.

[7] Note for for-profit FMC reporting entities: NZ IFRS 8 *Operating Segments* (NZ IFRS 8) requires disclosure of profit or loss for segments based on the measure reported internally to management. This may be different to the profit calculated in accordance with statutory financial reporting requirements. In most cases, we expect that any non-GAAP profit information disclosed will not differ from the segment reporting disclosures in the financial statements. If non-GAAP profit information is disclosed and it differs from the segment reporting disclosures in the financial statements, an explanation should be included justifying this difference. No explanation is required if the differences comprise only normal inter-segment eliminations or corporate expense allocations.

[8] We do not consider non-GAAP financial information to have been subject to audit or review merely by virtue of the adjustment or component being taken from audited or reviewed financial statements.

Reconciliation	• Entities should provide a reconciliation from the non-GAAP financial information to the most directly comparable GAAP financial information[9]. • Entities should itemise and explain each significant adjustment separately. • If reconciling items that are components of GAAP financial information, entities should identify them in the financial statements. • If you cannot extract a reconciling item directly from the financial statements, you should show how the number is calculated in the accompanying notes. • If presenting comparative non-GAAP financial information for a previous period, entities should provide reconciliation to the corresponding GAAP financial information for that previous period.
Consistency	• If an entity chooses to present non-GAAP financial information, a consistent approach should be adopted from period to period. • Where presented, entities should also provide the non-GAAP financial information for comparative periods. • If there has been a change in approach from the previous period, an explanation about the nature of the change, entities should provide the reasons for the change, and the financial impact of the change.
Unbiased	• Non-GAAP financial information should be unbiased. Entities should not use it to avoid presenting adverse information to the market or to over-emphasise favourable information.
One-off / non-recurring items	• Entities should not describe items that have occurred in the past or are reasonably likely to occur in a future period as 'one-off' or 'non-recurring.' For example, it may be misleading to describe items such as impairment losses and restructuring costs as 'non-recurring' or 'one-off' when they are generally of a recurring nature in many businesses and usually occur over the life of a business (although they may only arise every few years). • No 'cherry picking' adjustments. In the case of exclusion of non-recurring items, the exclusion should reflect *all* non-recurring items for the relevant period (i.e. both non-recurring charges as well as any non-recurring gains) regardless of whether they are related or not.

[9] An entity may disclose a reconciliation in each document where non-GAAP financial information is disclosed, or, make a direct reference to where this information is available. If an entity provides the reconciliation by reference, the reconciliation must be easily and readily accessible.

Disclosing pro-forma financial information

Pro-forma financial information is non-GAAP financial information that is intended to show the effects of proposed, completed or hypothetical events or transactions on an entity's financial position, performance, cash flows and/or prospects for illustrative purposes.

There are instances where providing investors with non-GAAP financial information in the form of pro-forma financial information may be necessary or useful to help with the assessment of a proposal.

For example, it may help investors deciding on a business combination to present pro-forma financial information showing how the business would appear based on historical information for the combined entities, had the transaction occurred at the start of the last financial year.

Pro-forma financial information can be misleading, particularly if there is no disclosure, or inadequate disclosure, of the basis of its preparation, or the differences between it and corresponding GAAP financial information.

As a form of non-GAAP financial information, the guidance outlined below should be applied in conjunction with the general principles set out earlier in this guidance note (see pages 9 - 10).

Guidelines on presenting pro-forma financial information

Guidance	Specific observations
Relevance	• Entities should avoid making adjustments that are not relevant to the proposal. For example, if the purpose of the proposal is to help users deciding on an acquisition of a business by illustrating how the business would appear based on the historical information for the combined entities had the transaction occurred at the start of the last financial year, the pro-forma financial information and related adjustments should only reflect the business combination and consolidation accounting of the combined entities. The adjustments should not extend beyond the relevant proposal. The information should also reflect the full transaction and not selected aspects of it. • In cases when complete pro-forma income statement is not required to be prepared, an entity should carefully consider whether it is appropriate to stop at the level of EBIT, EBITDA or operating profit. It is important that investors have enough information to understand the impact of a transaction on the funding and tax position of the entity. If your pro-forma income statement does not extend to net profit after tax, you should explain your reasons for not doing so, and the likely impact on funding, tax, amortisation and other items excluded from the pro-forma income statement. • Wherever possible, a pro-forma statement of financial position should include details of equity in addition to assets and liabilities. • We encourage entities to focus on material adjustments to support the user's understanding of the proposal.
Compilation	• Pro-forma financial information should: – be prepared on the same basis as the accounting policies of the entity; – use the most recent statutory financial statements as the starting point (either the half year, if available, or full year that has been reviewed or audited, as applicable); and – be based on reasonable and supportable assumptions
Presentation	• Disclosure of pro-forma financial information should be supported by: – full details of the principal assumptions used to prepare the information, including dollar values (as applicable); – details of any significant judgments made in choosing the most appropriate assumptions. Where there are a number of reasonably plausible alternative outcomes or scenarios, the entity should explain

these and consider providing a sensitivity analysis;

- an explanation of how it was compiled and the reasons for any departure from applicable accounting standards;
- a prominent statement to clarify that the information is for illustrative purposes only and does not represent the actual company's financial performance, position and/or cash flows; and
- a statement whether the pro-forma financial information has been subject to audit or review.

- When a range of pro-forma financial information is disclosed, a more favorable figure or fact within that range should not be given greater prominence.

Reconciliation

- The amount and nature of all material adjustments made to the statutory financial information to derive to the pro-forma financial information should be disclosed by way of reconciliation, together with the reasons for those adjustments. The reconciliation may be:
  - a line-by-line reconciliation of pro-forma financial information prepared with significant reconciling items, shown in a separate column and described through footnotes; or
  - a reconciliation of key items such as pro-forma profit and net assets (or other items such as current assets, non-current assets, current liabilities, non-current liabilities, revenue and expenses). This option would typically only be used when there are a limited number of reconciling items and each significant reconciling item is separately described.

Glossary of terms

Term	Meaning in this document
EBITDA	Net profit after tax plus interest, tax, depreciation and amortisation (EBITDA) with each of those items determined in accordance with GAAP
EBIT	Net profit after tax plus interest and tax
financial statements	Has the meaning given to it by section 6 of the Financial Reporting Act 2013
FMC reporting entity	Has the meaning given to it by section 451 of the Financial Markets Conduct Act 2013
GAAP	Generally accepted accounting practice, which has the meaning given to it by section 8 of the Financial Reporting Act 2013
GAAP profit or statutory profit	For for-profit FMC reporting entities this is the 'profit or loss' as defined in paragraph 7 of NZ IAS 1 *Presentation of Financial Statements* For PBE FMC reporting entities this is the "surplus or deficit" as defined in paragraph 7 of PBE IPSAS 1 *Presentation of Financial Statements*.
market announcements	Any announcements made to a securities exchange
non-GAAP financial measures	Has the meaning given to it in the Financial Market Conduct Regulations 2014
non-GAAP profit measures	Has the meaning given to it in the Financial Market Conduct Regulations 2014