HUNTON & WILLIAMS

BASELOAD

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Euro-Denominated Bonds: A Quick Guide for US Utility Issuers

Over the past couple of years, many US issuers have taken advantage of historically low interest rates in Europe by selling Euro-denominated debt. (Johnson & Johnson in May 2016, IBM and Berkshire Hathaway in March 2016, Apple in September 2015, ADM in June 2015, General Electric and Bristol-Myers in May 2015 and Coca-Cola in March 2015). In addition to the attractive rates, borrowing in Europe should allow US companies to diversify their base of debt investors geographically.

On June 20, 2016, Southern Power Company, a wholly-owned subsidiary of The Southern Company, issued €1.1 billion in green bonds. Eligible green projects included financing of, or investments in, solar and wind power generation facilities located in the United States. The offering was the first time a United States utility had taken advantage of the Euro market. We expect that additional energy issuers in the US will follow and thought it would be helpful to highlight a few of the most significant differences

between a Euro-denominated offering and a typical US based shelf takedown.

The Banks

Euro-denominated offerings are typically marketed by the UK affiliate of each investment bank. Similarly, the internal legal team at each bank supporting the offering will generally be from the bank's UK office. The underwriting agreement for these offerings will include a paragraph whereby the underwriters agree to accept the International Capital Markets Association (ICMA) Agreement Among Managers. Unlike the US practice, underwriters will either all sign the underwriting agreement on their own behalf, or one bank will sign on behalf of itself and all underwriters under power of attorney. Also, the Euro market's convention is to execute the underwriting agreement two days prior to close (so T+3 on a T+5 close), so issuers that wish to execute the underwriting agreement on the day of pricing will need to make the underwriters aware of that preference.

Unlike the US market where stabilizing efforts are made by the various bookrunners on the deal, the underwriting agreement will likely appoint a single bank to act as the "Stabilizing Manager" for the transaction.[1] Given this role, the description in the underwriting section of the prospectus supplement will likely need to be substantially revised. Further, it is common for the underwriters to request both a representation and covenant from the issuer that the issuer will not engage in any stabilization efforts during the course of the offering.

[1] See ICMA Primary Markets Handbook, Appendix A1, Agreement Among Managers.

The Terms

Almost without exception, US issuers that sell Euro-denominated debt apply to have the debt listed on the NYSE. Unlike certain hybrid securities of US utilities that are sold retail and listed on the NYSE, Euro-denominated debt generally will be deemed "debt" by the NYSE. Therefore, the underwriters will not be required to submit any representation letter to the NYSE with respect to post-offering holdings. NYSE Listed Company Manual Section 102.03 simply requires that "the debt issue must have an aggregate market value or principal amount of no less than $5,000,000."

Issuers should also be aware, and revise the disclosure accordingly, that the payment convention in Europe for fixed-rate debt is referred to as ACTUAL/ACTUAL as defined in the rulebook of the ICMA (as opposed to the 30/360 day count convention for fixed-rate debt in the United States).

The Underwriting Agreement

One very common additional provision present in many Euro-denominated underwriting agreements is a reference to certain "Bail-in Powers" of member states of the European Economic Area which have implemented the Bank Recovery and Resolution Directive (BRRD). The BRRD is Directive 2014/59/EU and gives resolution authorities in Europe wide-ranging

powers to manage failing financial institutions. (Under the BRRD, each member state is required to nominate a public administrative body to be the "resolution authority" responsible for exercising resolution powers).

The underwriting agreement will most often identify a "common depositary," which will (or together with an affiliate) also serve as the paying agent and registrar for the bonds in the UK. At closing, the authenticated global note will be delivered to this common depositary.

Many underwriters will request that the OFAC representation include references not only to the OFAC, but also any sanctions administered by the United Nations Security Council, the European Union and Her Majesty's Treasury.

Finally, most underwriting agreements for these Euro-denominated transactions include a provision with respect to "Judgment Currency." This addition is meant to clarify the point in time when an exchange rate will be set with respect to judgments in a currency other than US dollars. It is also meant to hold harmless the underwriters in case the underwriters are unable to purchase US dollars with the currency of the judgment award.

Taxes

Subject to a laundry list of exceptions, the bonds will be subject to a tax gross-up for non-US persons in the event that any withholding or deduction on payments in respect of the notes on account of any tax, assessment or other governmental charge is required to be deducted or withheld by the United States. However, there is also a corresponding redemption provision. To the extent there is any change in law such that the issuer becomes obligated to pay the additional amounts, the issuer may redeem the notes at par.

In most cases, the underwriting agreement will deem that any transfer taxes payable in connection with the sale of notes will be paid by the issuer. It is also common in the prospectus supplement for these Euro-denominated debt deals to notify purchasers that holders may be required to pay stamp taxes and other charges in accordance with the laws and practices of the country in which the debt is purchased.

Closing

Closing will generally take place on the fifth business day after the date of pricing (T+5). The issuer and the billing/delivering bank will need to work with Euroclear and Clearstream in order to determine whether an International Central Securities Depository (ICSD) Agreement between the issuer and Euroclear and Clearstream is required.[2] In the case of a Classical Global Note (CGN) that is deposited with a common depositary, an ICSD agreement may not be required.[3]

Closing through Euroclear or Clearstream does not require a telephone call on the morning of closing, as with a FAST closing at DTC. Instead, on the morning (London time) of closing, a contact at the billing and delivering bank will send a "green light" email to the working group, including the common depositary, stating that all of the conditions to closing have been met and that the parties are cleared to proceed with closing.[4]

Form SLT

In February 2011, the US Treasury released the final instructions for the reporting requirements of the Treasury International Capital Form SLT, the "Form SLT." It is a monthly report on cross-border portfolio investment in long-term marketable securities by US and foreign residents and is used by the US government

[2] Form available at: https://www.euroclear.com/dam/Brochures/NGN%20template%20Issuer%20ICSD%20agreement%20for%20a%20programme.

[3] See the ICMA's International debt securities in global registered form and in individual note form, Frequently Asked Questions, November 2009 for a discussion on a New Global Note (NGN) structure and the new safekeeping structure (NSS).

[4] For DTC closings there is a limit of $500 million per global debt security. See The Depository Trust Company, Operational Arrangements, p.5. When closing through Euroclear or Clearstream, we are not aware of any similar restriction on the size of a global security.

for formulating international financial and monetary policy. The form collects data on (1) the securities of a US person that are held by foreign resident investors (not through a US-resident custodian) and (2) a US person's investments in foreign securities that are not held by a US-resident custodian, in each case, when the aggregate amount of these securities exceeds $1 billion.

Form SLT treats all securities issued by a US person that are held through Euroclear and Clearstream as being held by foreign resident investors. Therefore, a US issuer of more than $1 billion of foreign bonds will likely be required to file a Form SLT on a monthly basis.

Final Thoughts and Potential Impact of Brexit

Issuers that are selling Euro-denominated debt for the first time are well advised to build additional time into their standard offering schedule. An inaugural offering in Europe will often necessitate an in-person roadshow. Underwriters' counsel will need to work closely with internal counsel in the UK in order to bring an issuer's standard underwriting agreement in line with what is expected for a Euro-denominated offering. With respect to closing mechanics, it is helpful to consider a more extensive form of closing memo, complete with timeline and funds flow, in order to ensure that both the pre-closing and closing of the trade proceed smoothly.

The impact of the June 23, 2016 vote in the United Kingdom on Euro-denominated debt transactions is yet to be seen. As has been reported widely in the press, the referendum was advisory rather than mandatory and has no immediate legal consequences. What is clear is that financial markets will likely continue to be volatile, which may affect the timing of any potential transaction.

Don't Get Your Wires Crossed on Utility Deals: Recent Communications Issues for Treasury, IR and Underwriters

A securities offering requires a tremendous amount of coordination by the utility, its treasury department, investor relations team, internal counsel and outside counsel, as well as the underwriters and their counsel. We thought it might be helpful to review some recent communications issues in the context of utility securities offerings. Planning and coordination are key in order to comply with the myriad of regulations and standards of liability imposed by the federal securities laws, the SEC, any applicable stock exchange and other regulatory authorities.

What is an "Offer"?

It is clear that some materials in connection with a utility's securities offering are "offers" of securities and are regulated as such: the offer document, any term sheet or a deal roadshow assembled and presented as part of the offering

process. But often the other communications which are close in proximity to the offering give rise to thorny determinations as to whether they, too, are offers of the securities.

Section 2(a)(3) of the 1933 Act defines the term "offer" expansively; it includes "every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value." Any publicity that may "contribute to conditioning the public mind or arousing public interest" in an offering can constitute an offer under the 1933 Act.[1]

Rule 168

The SEC has over the years adopted many safe harbors from the definition of "offer". And one of the most critical of these to a utility conducting a securities offering is Rule 168 under the 1933 Act. Rule 168 is a non-exclusive safe harbor that is available only to reporting issuers[2] with a history of making similar public disclosures. It permits a reporting issuer to make continued regular release of "factual business information" and "forward looking information," but not information about an offering or information released as part of offering activities. Rule 168 is not available to underwriters.

The Rule 168 safe harbor is designed to permit ongoing communications with the market, such as press releases, earnings releases, conference calls, earnings guidance and other information released in accordance with an issuer's past practices. The issuer must have previously released factual information in the ordinary course of business, and the timing, manner and form of information must be consistent with prior practice.

One common use of Rule 168 is to exclude earnings guidance from the offering materials. If guidance is revised in proximity to an equity offering, there is a risk that it may be deemed to be included in the offering materials, even if it is not included in, or incorporated by reference by the prospectus. Most utilities could utilize the safe harbor of Rule 168 in an equity offering if (1) the company has previously disseminated guidance in the ordinary course of business and (2) the timing, manner and form in which the guidance is released is consistent with the past such releases. For the utility industry, Rule 168 is extremely helpful. There are many regularly scheduled industry conferences (e.g. EEI events) or investment banking events at which utilities regularly present and reaffirm/ update earnings guidance. These events are in addition to the other regularly scheduled occasions—such as quarterly earnings calls—where utilities announce guidance. To the extent an equity deal is launched contemporaneously or soon after one of these events which the issuer has traditionally utilized to present guidance, the guidance should meet the "timing, manner and form" test of Rule 168. For a more complete discussion, see also the January 2013 Baseload for "*Offering Guidance: What to Consider Before Your Next Equity Offering*."

Another area where we commonly encounter the use of Rule 168 is in connection with non-deal road shows by utility issuers. These road shows are often designed by the investor relations team in order to update or raise the issuer's profile with the investment community, outside the

[1] *See Publication of Information Prior to or After the Effective Date of a Registration Statement,* Release No. 33-3844 (Oct. 8, 1957).

[2] An issuer that is required to file reports pursuant to Section 13 or Section 15(d) of the 1934 Act.

context of a securities offering. But care must be taken that any such presentation is not deemed part of a subsequent offering.

The Rule 168 safe harbor permits, under certain circumstances, an issuer to conduct a non-deal road show with confidence that the presentation will not be deemed an "offer" under the securities laws. The "timing, manner and form" of the non-deal road show must be consistent with similar past presentations. Certain non-deal road shows, however, occur without the benefit of Rule 168 and with the possibility, subject to market conditions, of launching a transaction in the near future. Assuming Rule 168 is not available, if a deal is launched on the heels of a non-deal road show, it is possible that the non-deal road show could be construed as an offer of securities (even though the slides make no reference to the upcoming offering).

A non-deal road show done in proximity to a securities offering may constitute a written offer, with the slides deemed a "free writing prospectus" or a prospectus. To avoid this result, counsel should explore the availability of the Rule 168 safe harbor or, alternatively, include the Rule 433 legend and agree that, given the proximity of the non-deal road show to a potential offering, the road show could be deemed an offering of securities. See also the January 2014 Baseload for "*Electronic Road Shows - What to Leave In, What to Leave Out*."

Regulation FD

Regulation FD addresses the selective disclosure of information by issuers. Regulation FD provides that when an issuer discloses material non-public information to certain individuals or entities — generally, securities market professionals such as stock analysts, or holders of the issuer's securities who may well trade on the basis of the information — the issuer must make public disclosure of that information.

Regulation FD is always a concern during an offering of securities.[3] The issuer needs to confirm that if material, nonpublic information is being shared, it is being shared in a manner that is compliant with the requirements of Regulation FD. While the SEC did not define what is "material," the SEC did enumerate in the final release for Regulation FD seven categories of information that are more likely to be considered material:

1. Earnings information
2. Mergers, acquisitions, tender offers, joint ventures or changes in assets
3. New products of discoveries or developments regarding customers or supplies (e.g. the acquisition or loss of a contract)
4. Changes in control or in management
5. Changes in auditor or auditor notification that the issuer may no longer rely on an auditor's audit report
6. Events regarding the issuer's securities (e.g. defaults on senior securities, calls of securities for redemption, repurchase plans, stock splits or changes in dividends, changes to rights of security holders, public or private sales of additional securities)
7. Bankruptcies and receiverships[4]

[3] See also *Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Netflix, Inc., and Reed Hastings*, Release No. 69279 (Apr. 2, 2013) for the SEC's explanation of how to use social media for Regulation FD compliance.

[4] See *Selective Disclosure and Insider Trading*, Release No. 33-7881 (Aug. 15, 2000).

Note also that the list of events that the SEC requires issuers to disclose on Form 8-K is also representative of what are presumptively material events.

One issue that frequently comes up during a utility offering is whether the issuer should file the preliminary prospectus prior to distributing the prospectus to potential investors. While most communications in connection with an offering of securities registered under the 1933 Act are exempt from the requirements of Regulation FD,[5] issuers will still want to review a preliminary prospectus in order to determine whether any information therein is both material and nonpublic. If so, despite the exception for registered offerings in Regulation FD, issuers may prefer to file such a prospectus with the SEC prior to providing the document to potential investors.

Note that there is no equivalent exemption for private offerings under Regulation FD. As such, for utility issuers that are considering a Rule 144A transaction, deal participants must conduct a thorough review of the offering materials in order to confirm that no material, nonpublic information is being shared by the issuer by any means that is not compliant with Regulation FD.

Regulation FD enforcement actions have made headlines in the past several years. In September 2013, the SEC announced that it had brought—and settled—a cease-and-desist case under Regulation FD against a former vice president of Investor Relations at First Solar, Inc. In this case, the executive had selectively disclosed that the company was unlikely to receive financing under a conditional loan from the Department of Energy. Even though the company had not yet issued its public announcement regarding the DOE loan, the executive and his subordinate had phone conversations with more than 30 analysts and investors, "effectively signaling" that First Solar would not receive one of the loan guarantees.

Issuer Websites

Another focus of an issuer and the underwriters during a utility offering is the information contained on the issuer's website and, in particular, on the Investor Relations page of the website.[6] As the SEC described in 2008 in its "*Commission Guidance on the Use of Company Web Sites*":[7]

> The antifraud provisions of the federal securities laws apply to company statements made on the Internet in the same way they would apply to any other statement made by, or attributable to, a company. This includes postings on and hyperlinks from company web sites that satisfy the relevant jurisdictional tests…..Accordingly, a company should keep in mind that applicability of the antifraud provisions of the federal securities laws, including Exchange Act Section 10(b) and Rule 10b-5, to the content of its web site.

It is important to be sure that nothing on the website might unintentionally amount to a written

[5] Except in certain limited circumstances, Regulation FD does not apply to an issuer's communications and disclosures made in connection with an offering of securities registered under the 1933 Act. This exemption is not available for certain registered shelf offerings, including secondary offerings, employee benefit plan offerings and offerings pursuant to warrants and other convertible securities.

[6] Note that Section 307.00 of the NYSE Listed Company Manual requires that listed companies have and maintain a publicly accessible website.

[7] See *Commission Guidance on the Use of Company Web Sites*, Release No. 34-58288 (Aug. 1, 2008).

offer and therefore be treated as a "free writing prospectus" under the 1933 Act.[8] As described above, Rule 168 can be useful in order to exclude information from the definition of "prospectus" under the 1933 Act that is regularly released factual business information or forward-looking information.

Securities Offering Reform in 2005[9] also promulgated Rule 433(e)(2). This rule excludes as an offer "historical issuer information that is identified as such and located in a separate section" of a website that contains historical issuer information, provided that the issuer has not incorporated the information into an offering document and the issuer and the underwriters have not otherwise used or referred to the information in connection with the offering.

Company counsel should participate in formulating a process relating to public communications that includes periodic website (and social media) maintenance. In a perfect world, company counsel should review content before it is posted on an issuer's website or social media accounts. And during the course of a securities offering, the various teams at the issuer need to have a heightened focus on any materials that will be posted to the website. Further, the issuer's investor relations department (rather than the marketing department) should be responsible for the investor relations portion of the issuer's website. The investor relations department may be more sensitive to securities law matters, including compliance with Regulation FD (discussed above).

Rule 144A and General Solicitation

Effective September 2013, in accordance with the "Jumpstart Our Business Startups Act" (the "JOBS Act"), the SEC amended Rule 144A to permit general solicitation and general advertising, provided that actual sales are only made to persons that are reasonably believed to be "qualified institutional buyers" (QIBs). As a result, issuers and underwriters now have enhanced flexibility to publicize a Rule 144A offering without loss of the exemption from registration. Prior to the revision, one of the conditions was that the securities both be ***offered*** and sold only to persons the seller and any person acting on the seller's behalf reasonably believe are QIBs. Note also that the SEC has clarified that, in addition to the issuer, the initial purchasers and other distribution participants may conduct the general solicitation.[10]

The new rules allow issuers and their agents to communicate with prospective investors in Rule 144A deals with no limit on the method of communication or the number or type of investors reached. Issuers may now use blast emails, advertisements, articles and other communications published in newspapers or magazines, or on the Internet or television. The liberalization also allows communications about these kinds of offerings at conferences, promotional seminars or other meetings. Despite the new flexibility, however, in our experience,

[8] See *SEC Interpretation: Use of Electronic Media*, Release No. 33-7856 (Apr. 28, 2000) for SEC guidance regarding an issuer's liability for website content.

[9] See *Securities Offering Reform*, Release No. 33-8591 (Dec. 1, 2005).

[10] SEC Compliance and Disclosure Interpretations, Securities Act Rules, Question 138.03 (Nov. 13, 2013).

most 144A offerings that are being done in the utility space continue to prohibit general solicitation, consistent with prior practice, by the issuer and often the initial purchasers as well, preventing the parties to the deal from utilizing the new flexibility with respect to Rule 144A.[11]

[11] Section 18 of the 1933 Act preempts state "Blue Sky" laws with respect to offerings of "covered securities." Section 18 includes as covered securities only securities of ***reporting*** issuers offered and sold in Rule 144A transactions. The states themselves exempt offers and sales to sophisticated institutional investors by all issuers. But general solicitation could also constitute offers to non-institutional investors,and only three states effectively exempt offers to those investors in a Rule 144A context. Accordingly, use of broad-reaching general solicitation in Rule 144A offerings by non-reporting issuers could require registration under certain state Blue Sky laws. It is unclear whether any such state would pursue an enforcement action in such a case.

Conclusion

The legal framework that applies to communications during a securities offering has become increasingly complex. Significant nuances exist in some of the most critical legal determinations. The various constituencies of a utility's offering of securities—treasury, IR, investment banks and legal teams—are well-advised to communicate early and often during the process in order to ensure that all parties are in agreement with respect to the treatment of the many moving parts.

Non-GAAP Measures: New SEC Guidance Signals Increased Scrutiny

On May 18, 2016, the SEC released new guidance regarding the use of non-GAAP measures in the form of twelve new or updated Compliance and Disclosure Interpretations (C&DIs).[1] This new guidance comes on the heels of several critical comments from SEC Chairman Mary Jo White and other SEC officials on the increased use and potentially misleading nature of such measures.[2]

The C&DIs address Regulation G, which concerns all public disclosures of information that contains non-GAAP financial measures made by 1934 Act registrants and Item 10(e), which regulates the use of non-GAAP financial measures in filings made under the 1933 or 1934 Acts. Collectively, the new C&DIs suggest that there will be increased scrutiny on the usage and types of non-GAAP disclosures by the SEC staff.

The new guidance addresses how certain non-GAAP measures can be potentially misleading under Rule 100(b) of Regulation G. In particular, the staff notes that certain adjustments, although not explicitly prohibited, could cause the non-GAAP measure to be misleading. For example, the presentation of a performance measure that excludes normal, recurring, cash operating expenses necessary

[1] For a copy of the C&DIs, *see* https://www.sec.gov/divisions/corpfin/guidance/nongaapinterp.htm.

[2] *See* "SEC Signals It Could Curb Use of Adjusted Earnings Figures." *The Wall Street Journal* (March 16, 2016), *available at* http://www.wsj.com/articles/sec-scrutinizing-use-of-non-gaap-measures-by-public-companies-1458139473.

to operate a registrant's business could be misleading.[3] Additionally, the staff clarifies that a non-GAAP measure can be misleading if it is presented inconsistently between periods.[4] Also, 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 potentially violate Regulation G.[5] Lastly, the C&DIs address a hypothetical situation in which a company 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 were billed. The staff notes that non-GAAP measures that substitute individually tailored revenue recognition and measurement methods for GAAP measures could violate Rule 100(b) of Regulation G, and further, that other measures that use individually tailored recognition and measurement methods for financial statement line items other than revenue may also violate Rule 100(b).[6]

The C&DIs also clarify whether certain non-GAAP measures may be presented on a per share basis pursuant to Item 10(e). The staff notes that non-GAAP liquidity measures that measure cash generated must not be presented on a per share basis in documents filed or furnished with the SEC. 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. Going forward, the staff is expected to focus on the substance of the non-GAAP measure and not management's characterization of such measure when analyzing such disclosure.[7] The staff also notes that free cash flow (e.g. cash flows from operating activities less capital expenditures) is a liquidity measure that must not be presented on a per share basis and EBIT and EBITDA (along with similar measures) must not be presented on a per share basis.[8]

The new guidance also mandates equal prominence between non-GAAP measures and the corresponding GAAP measurements under Item 10(e)(1)(i), setting forth the staff's view that GAAP measures must be presented first and described narratively in a manner similar to that of the comparable non-GAAP measures. The guidance will effect, among other things, disclosures made in annual and quarterly reports and earnings releases. The staff notes in particular that a company is prohibited from:

- Presenting a full income statement of non-GAAP measures or presenting a full non-GAAP income statement when 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)

[3] SEC Compliance and Disclosure Interpretation, Question 100.01(May 17, 2016), *available at* https://www.sec.gov/divisions/corpfin/guidance/nongaapinterp.htm.

[4] SEC Compliance and Disclosure Interpretation, Question 100.02.

[5] SEC Compliance and Disclosure Interpretation, Question 100.03.

[6] SEC Compliance and Disclosure Interpretation, Question 100.04.

[7] SEC Compliance and Disclosure Interpretation, Question 102.05.

[8] SEC Compliance and Disclosure Interpretation, Question 102.07 and Question 103.02.

- 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
- 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.[9]

[9] SEC Compliance and Disclosure Interpretation, Question 102.10.

Lastly, the staff clarifies that registrants should provide income tax effects on their non-GAAP measures depending on the nature of such measures. If a measure is a liquidity measure that includes income taxes, the guidance suggests that it might be acceptable to adjust GAAP taxes to show taxes paid in cash. If a measure is a performance measure, the staff notes that companies 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.[10]

These C&DIs make clear that the SEC will be taking a more aggressive approach in reviewing a company’s use of non-GAAP measures, and we can expect to see more staff comment letters in the coming months. Companies should review their current disclosure practices in light of this new guidance.

[10] SEC Compliance and Disclosure Interpretation, Question 102.11.

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