European Securities and Markets Authority

Final Report

ESMA Guidelines on Alternative Performance Measures

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List of abbreviations and acronyms used in this report

APM	Alternative Performance Measures
CP	Consultation Paper
CESR	Committee of European Securities Regulators
EC	European Commission
EEA	European Economic Area
EECS	European Enforcers Coordination Session
EU	European Union
ESMA	European Securities and Markets Authority
GAAP	Generally Accepted Accounting Principles
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
MAR	Market Abuse Regulation
CA	Competent Authority
SMSG	Securities and Markets Stakeholder Group

Executive Summary

Reasons for publication

The European Securities and Markets Authority (ESMA) issued in February 2014 a Consultation Paper (CP) on Guidelines on Alternative Performance Measures (APM) ('guidelines') to replace the Recommendation issued by the Committee of European Securities Regulators (CESR) in 2005. The guidelines will apply to issuers or persons responsible for the prospectus.

This report provides an overview of the feedback received from stakeholders and from the ESMA Securities and Markets Stakeholder Group (SMSG) on issues related to APMs as well as the ESMA response to it. The final guidelines presented in Annex IV take into account the comments and suggestions raised by respondents.

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ESMA welcomes the feedback received on the proposed guidelines, underlining the importance of the establishment of principles to be followed by issuers or persons responsible for the prospectus who provide APMs in documents containing regulated information or prospectuses. While users who responded to the CP were very supportive of the proposed guidelines as they believed that these would result in useful information about APMs, issuers considered that compliance with the proposed guidelines would increase the disclosure overload in documents containing regulated information and prospectuses.

To respond to the criticism from respondents, ESMA revised the scope of the proposed guidelines and amended the definition, the presentation and the reconciliation principles for the APMs. Financial statements have been excluded from the scope, considering that they are already covered by the applicable financial reporting framework or latest amendments to it. ESMA has also relieved issuers or persons responsible for the prospectus from the obligation to provide an Appendix with all APMs and allowing issuers to make reference to other documents when complying with these guidelines.

A majority of respondents agreed with extending the scope of the proposed guidelines to prospectuses and other related documents which include APMs. Therefore, the scope was amended to include prospectuses and the final guidelines contain new paragraphs to address the specificities of the prospectus regime.

Next steps

Following the translation of the guidelines in Annex IV into the official languages of the EU, the final texts will be published on ESMA's website in the course of 2015.

The guidelines will become effective for all documents issued on or after the effective date of 3 July 2016.

1 General remarks

1. The objective of the CP was to inform market participants about the background of ESMA's decision to revise the CESR Recommendation on Alternative Performance Measures and to seek opinion of stakeholders on the proposed ESMA guidelines.

2. This final report provides an overview of the responses received by ESMA to the CP, describes any material changes to the proposed guidelines set out in Annex IV of the CP (or confirms that there have been no material changes) and explains the reasons for this in light of the feedback received.

3. The comment period closed on 14 May 2014 with 62 responses received from a broad range of stakeholders, with the majority from the following categories: preparer representatives (46%), accounting bodies and auditors (25%) and user representative bodies (14%). Other responses came from standard setters, government bodies and the SMSG. A detailed list of the respondents, grouped by category, is provided in Annex I.

4. The SMSG is a key ESMA stakeholder consultative body composed of 30 individuals from 17 Member States and representing academics, consumers, financial institution employees, financial market participants, small and medium sized enterprises as well as users of financial information. This group facilitates consultation with stakeholders in areas relevant to ESMA's tasks such as the development of technical standards and guidelines. Article 37(1) of the ESMA Regulation provides that ESMA shall consult the SMSG to give its advice on any consultation related to guidelines. The SMSG 'Position Paper' on this CP is included in Annex III.

5. The answers received on the CP are available on ESMA's website [1] unless respondents requested otherwise. ESMA is most grateful to all who took the time to bring their contribution to the consultation process. Some answers were more general, while others were very specific to the questions asked. The number of responses received on each question is included at the beginning of the individual feedback per question. For each question, ESMA included in the feedback statement a summary of the main messages received on the proposed guidelines and the feedback provided by ESMA.

Overall messages

6. Generally, most respondents were supportive of ESMA's initiative to issue guidelines. The SMSG and the users of financial information believed that the information provided by the application of the proposed guidelines would be useful for the decision making process of investors as the compliance with these guidelines ensure that issuers or persons responsible for the prospectus will provide relevant disclosures for the understanding of the APMs used by issuers or persons responsible for the prospectus.

[1] http://www.esma.europa.eu/consultation/ESMA-Guidelines-Alternative-Performance-Measuresresponses

7. However, many respondents had the perception that compliance with the guidelines could lead to a disclosure overload in the publication of regulated information. Therefore, those stakeholders believed that some improvements were necessary to achieve the goal of the proposed guidelines.

8. Although ESMA acknowledges that the compliance with the proposed guidelines may lead to an increase in the information included in documents containing regulated information, it also strongly believes that such compliance will lead to a better understanding of the APMs used by users of that information. ESMA believes that only relevant information will be provided by issuers or persons responsible for the prospectus as they shall apply the materiality concept defined by the applicable financial accounting framework, when they follow the principles established in the guidelines.

9. In this context, ESMA took into account the findings from recent studies carried out in Sweden[2] and the United Kingdom.[3][4] Those studies demonstrate the usefulness of financial information and point out that users are more concerned about the use of boilerplate disclosure rather than the extent of disclosure of financial information. In addition, they suggest that emphasis should be given to improvements in the quality of disclosure rather than to their location in the financial report.

10. In addition, ESMA took into account the concerns expressed and the suggestions provided by respondents, and amended the proposed guidelines clarifying the scope of the APM, providing waivers and reliefs to some of the requirements and allowing more flexibility for issuers or persons responsible for the prospectus when complying with the guidelines. In that respect, the final guidelines enable issuers to comply through the use of adequate references to documents where the information required by the guidelines may be found. ESMA believes that this relief will significantly reduce the compliance burden for issuers.

11. ESMA considers that the changes made will be sufficient to ensure that respondents' concern on the disclosure overload is mitigated. As the quality of the information provided is ultimately the responsibility of issuers or persons responsible for the prospectus, ESMA encourages issuers or persons responsible for the prospectus to provide relevant and entity specific information, apply the materiality concept as defined in the applicable financial reporting framework (IFRS or national GAAP) and avoid boiler-plate disclosures when following the provisions established in the guidelines.

Application of the guidelines

12. In order to provide sufficient time for issuers or persons responsible for the prospectus to adapt their internal procedures and reporting systems, and for CAs to

[2] Decision usefulness explored: An investigation of capital market actors' use of financial reports; Swedish Enterprise, 2014
[3] Lab insight report: Towards Clear & Concise Reporting, Financial Reporting Council, August 2014
[4] Lab project report: Accounting policies and integration of related financial information, Financial Reporting Council, July 2014

incorporate these guidelines into their supervisory practices, ESMA decided to set the effective date of application of these guidelines on the 3 July 2016.

2 Feedback Statement

13. This section provides a summary of the responses, by identifying the main comments from the respondents and ESMA's view on those responses, together with changes to the guidelines, where appropriate. When summarising the answers to the CP, ESMA used the formulation 'proposed guidelines'. All other references are made to the final guidelines included in this report.

14. In view of the requirement to request the SMSG for an opinion or advice before issuing Guidelines, ESMA has considered the points raised by the SMSG and addressed them in its response to every question in this feedback statement and the final guidelines. In line with its mandate, ESMA paid careful attention to the response of users in order to improve investor protection and the transparency of financial information provided by issuers or persons responsible for the prospectus.

Q1: Do you agree that the ESMA [draft] guidelines should apply to all issuers defined as a legal entity governed by private or public law, other than Members State or Member State's regional or local authorities, whose securities are admitted to trading on a regulated market, the issuer being, in the case of depository receipts representing securities, the issuer of the securities represented regardless of the financial reporting framework they use to report? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
35	12	5	15	2	0	1

15. Most respondents considered that the application of the same requirements to all issuers is reasonable and will strengthen and promote transparency of documents published by issuers. In their view, a consistently application of the framework enhances public confidence in financial reporting, comparability between entities and over time, as well as understandability by users.

16. Three respondents considered that the scope of the proposed guidelines was consistent with the Transparency Directive and Market Abuse Regulation, but questioned the proposed exclusion of Member States. They suggested ESMA to identify and explain any difference of scope for the sake of clarity.

17. **ESMA's response:** ESMA welcomes the broad support on the scope of issuers for which the guidelines apply. Regarding the Member State's exclusion, ESMA recalls that the documents published by Member States and regional or local authorities are subject to rules and principles that are not harmonized at European level and in

relation to which CAs have limited powers of enforcement, if any. As such, ESMA has decided not to include those issuers in the scope of the final guidelines.

18. When amending the final version of the guidelines, ESMA considered the changes included in the definition of an issuer in accordance with the amended Transparency Directive[5] and, consequently, updated this definition to include 'natural persons' within its scope of application. The final guidelines were also amended to include persons responsible for the prospectus considering the support received to include prospectuses.

Q2: Do you agree that the ESMA [draft] guidelines should apply to APMs included in:

a) financial statements prepared in accordance with the applicable financial reporting framework, that are made publicly available, and

b) all other issued documents containing regulated information that are made publicly available?

If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
45	12	7	18	3	4	1

19. Respondents had mixed views about the application of the proposed guidelines to APMs included in documents containing regulated information. Whereas some respondents believed that the scope of the proposed guidelines should be wide enough to include all documents published by issuers, others believed it should be narrowed to capture only the information required to be published according to the requirements in the Transparency Directive.

20. Three respondents considered that the proposed guidelines would have implications for the audit of financial statements and suggested that users should be informed whether APMs have been audited or not. They proposed that ESMA provides guidance on how issuers should report APMs in their financial statements.

Financial statements

21. All user representatives and the SMSG agreed that APMs should be consistently used and presented in all documents published by issuers, so that the guidelines should be applied to all documents containing regulated information.

[5] Directive 2013/50/EU of the European Parliament and of the Council of 22 October 2013.

22. Seven respondents (mainly preparers) raised concerns about the application of the proposed guidelines to APMs included in financial statements and made reference to segment reporting as required by IFRS 8 *Operating Segments*. In their view, financial statements should be scoped out as providing guidance related to the application of accounting standards should be dealt with by standard setters.

23. A number of respondents recalled the IASB's project on the 'Disclosure Initiative' and encouraged ESMA to coordinate with the IASB to amend existing requirements where necessary in order to align respective efforts in developing a consistent framework covering APMs.

24. Finally, respondents suggested to amend some of the terminology in the proposed guidelines and recommended to use the term 'half-yearly financial report' instead of 'interim management statements' as the latter is not used in the Transparency Directive.

Other documents

25. Twenty-two respondents (10 preparers, 5 accounting bodies and auditors, 2 users, 3 regulators, 2 standard setters) expressed their concerns about the extension of the scope of the proposed guidelines to 'all other issued documents containing regulated information' (question 2 b). Auditors considered that ESMA should clarify the scope of the proposed guidelines so that non-regulated information is not captured inappropriately. In their view, extension to all documents would conflict with the intended scope of the proposed guidelines and be 'unworkable in practice'. They also feared it would lead to an extension of the scope of IFRS information from financial reporting to all publications from companies on financial issues.

26. **ESMA's response:** ESMA took note of the concerns raised by respondents in relation to the interaction between the proposed guidelines and financial statements and has thus excluded financial statements prepared in accordance with the applicable financial reporting framework from its scope.

27. When taking such decision, ESMA has considered the recent amendments made to IAS 1 – *Presentation of Financial Statements* as well as the IASB long-term research project which deals with disclosure principles. In this context, ESMA believes that the amendments to IAS 1, proposed by the IASB, will solve most of the issues identified and will promote the transparency of APMs included in financial statements by ensuring that those measures are comparable, consistent and less prominent than measures defined in the applicable financial reporting framework. ESMA is of the view that most APMs used in financial statements are within the scope of those amendments, as those measures are mainly presented in primary financial statements and are calculated by adding or subtracting figures from measures defined by the applicable financial reporting framework, thus constituting sub-totals.

28. ESMA also believes that even when APMs are presented in the notes to the financial statements, the provisions in the standard requiring the cross-reference between the

notes and, in some cases, reconciliations (for instance in the case of IFRS 8) will allow users of financial information to understand the components of those measures.

29. Although financial statements are scoped out of the final guidelines, ESMA encourages issuers or persons responsible for the prospectus who include APMs in financial statements to provide information to users on the relevance of such measures for their decision making process. Even though such requirement is not mandatory in the amendments to IAS 1, ESMA strongly believes that this information is of major relevance to investors when making informed decisions.

30. ESMA takes note of the concern expressed regarding the application of the proposed guidelines to all other issued documents containing regulated information and understands that the wording might be too generic. In this respect, ESMA has clarified the scope of application in paragraphs 3 and 4 of the final guidelines and included the reference to the legal provision in the Market Abuse Regulation (MAR) that requires issuers to provide this information to the market. Examples of regulated documents which might contain APMs on which these guidelines are likely to be applied include ad-hoc disclosure containing financial earnings results.

31. To address the concerns of the respondents about the increase of disclosures in documents containing regulated information, ESMA clarified in the final guidelines that incorporation per reference is permitted in all cases (not only in ad-hoc disclosures). ESMA believes that this practical expedient will avoid repetitions and provide sufficient relief for issuers.

Q3: Do you believe that the ESMA [draft] guidelines should also be applicable to prospectuses and other related documents, which include APMs (except for pro-forma information, profits forecasts or other measures which have specific requirements set out in the Prospectus Directive or Prospectus Directive implementing regulation)? Please provide your reasons

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
38	12	6	16	3	0	1

32. A majority of respondents (23) including all user representatives, auditors, a number of preparers (6) and the SMSG agreed with an extension of the scope of the proposed guidelines to prospectuses and other related documents which include APMs as it would increase the consistency in financial information published.

33. The SMSG strongly believed that the proposed guidelines should apply to APMs published in prospectuses and related documents and that there was no objective reason to exclude them from transparency requirements. In its view, it is important and helpful for investors to be able to check the consistency of the information (and

financial data) in prospectuses with the information published in the financial statements after those issuers are listed on regulated market.

34. All accounting bodies and auditors' representatives but one agreed with the application of the proposed guidelines to prospectuses provided that the scope of APMs was appropriate, the application modalities clarified and some exceptions to its scope provided. As the Prospectus Directive regulates the way certain financial measures (e.g. pro-forma information, profits forecasts and other specific measures) should be prepared and presented, it would be inappropriate to apply these guidelines to those specific financial measures. As such, auditors recommended ESMA to consider either extending the scope of the final guidelines to specific sections of the prospectus or defining sections or types of information to be excluded from its scope.

35. Thirteen respondents (mainly issuers) considered that the proposed guidelines were not the appropriate vehicle to introduce new requirements in relation to prospectuses as the Prospectus Directive and its implementing acts were sufficient and appropriately excluded from the CESR Recommendation on APMs. As the European prospectus regime is complete and presents a detailed approach of all categories of information to be produced by issuers, they considered that additional disclosures from the proposed guidelines would add complexity and redundancy to the process. They recalled that the ESMA Recommendation on prospectuses (ESMA/2013/319) already deals with this topic and feared that an extension of the guidelines to prospectus would duplicate existing requirements and generate additional burden when drawing up prospectuses.

36. **ESMA's response:** ESMA acknowledges the support for including prospectuses and other related documents in the scope of the guidelines, and thus amended the scope accordingly. The final guidelines contribute to a consistent and comprehensive approach on the use of APMs regardless where these measures are presented. ESMA believes that the final guidelines contribute to increasing consistency between the principles applicable to financial information used before and after the admission to trading on regulated markets.

37. Furthermore, ESMA considers that the convergence of the requirements in both directives and supervisory practices will foster investor protection, avoid regulatory arbitrage, contribute for a single rulebook and promote a common, uniform and consistent application of the requirements across different countries.

38. In order to address the specificities of the prospectus regime, the final guidelines were amended to ensure their applicability to issuers under the PD regime and all persons responsible for drawing up prospectuses. The guidelines take into account that the PD regime already sets out disclosure requirements for some elements which can be under the definition of APMs and do not require the application of the guidelines in those cases.

Q4: Do you believe that issuing ESMA guidelines constitute a useful tool for dealing with the issues encountered with the use of APMs? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
45	14	5	21	2	2	1

39. Respondents, including all user representatives and the SMSG, generally considered that the proposed guidelines were a useful tool to deal with APMs and would contribute to an improvement in the quality of the financial information provided by issuers. Some respondents shared ESMA's view expressed in the CP that sometimes issuers use APMs to present a confusing or too optimistic picture of their performance and can therefore be misleading if they are inconsistently calculated or presented.

40. However, eight respondents were of the view that the proposed guidelines were too prescriptive and would have preferred a more principle-based set of guidelines. While recognizing that proposed guidelines constitute a useful tool for users and national regulators, those respondents advocated a more proportional use of the guidelines, in order to enable issuers to adapt its application depending on the APMs used, thus avoiding additional burden.

41. Other respondents considered that ESMA neither justified nor provided empirical evidence on the reasons why the CESR Recommendation should be replaced by ESMA Guidelines. They proposed that ESMA differentiates the issues encountered from a lack of adherence or from eventual loopholes in the previous recommendation. They also suggested that ESMA issues 'recommendations' rather than guidelines under Article 16 of the ESMA Regulation.

42. **ESMA's response:** ESMA acknowledges that the enforcement experience from the CAs and academic studies confirms that issues related to APMs continue to occur across Europe, despite the publication of the CESR Recommendation in 2005.This was illustrated in the ESMA letter addressed recently to the IASB on IAS 1[6] where ESMA recalled the significant divergence observed in the presentation of the primary financial statements.

43. As a response to the criticism, when preparing the final guidelines, ESMA decided to highlight the key findings and conclusions from recently published reports released by CAs and academic studies.

44. In 2012, a survey of the use of APMs carried out in Ireland[7] concluded that there was a large divergence in the use and definitions of some APMs across issuers such as

[6] http://www.esma.europa.eu/system/files/2013-1555_esma_comment_letter_to_the_ifrs_ic_on_application_of_ias_1.pdf
[7] http://www.iaasa.ie/publications/APM2012.pdf

EBITDA earnings, especially in respect to the items included or excluded from the earnings component. Furthermore, the APM's were not reconciled to IFRS figures.

45. In 2014, a thematic review on the use of alternative financial performance indicators in press releases in 2013 in the Netherlands[8] concluded that the use of alternative financial performance indicators was increasing, but their application was less consistent.

46. Furthermore, a global survey on the disclosure of adjusted performance measures was conducted among investment professionals in 2014[9] and concluded that APMs were useful even though issuers could improve the quality of their APM reporting with clearer descriptions of the adjustments and more adequate information on the reasons for those adjustments.

47. Several academic studies have also stressed the benefits of APMs and underlined that issuers make extensive use of APMs but that the provision of reconciliation is an exception. Researchers show sympathy for more regulation on non-GAAP-measures to increase comparability and transparency. The German empirical study by Bassen et al. (2012)[10] suggests an increasing transparency and understanding of APMs if reconciliations and explanations are given. Similar observations could be found in empirical studies by Küting and Heiden (2002)[11] and by Hitz and Jenniges (2008)[12]. Additionally, several behavioural studies[13] highlighted the positive effects of explained APMs and their reconciliations on particular investors groups.

48. ESMA has considered these arguments and continues to believe that, in view of its experience and in line with the legal powers granted by the ESMA Regulation, guidelines are the appropriate tool to update CESR Recommendation on this topic.

49. When taking this decision, ESMA considered all the legal instruments provided for under the ESMA Regulation. Considering that guidelines are the only legal instrument that can be addressed to financial market participants (issuers or persons responsible for the prospectus), ESMA decided to reissue the principles contained in the previous CESR recommendation as Guidelines under Article 16 of ESMA Regulation.

50. In order to address the concerns expressed by respondents that the proposed guidelines should be more principles-based and less prescriptive, ESMA has amended some of the provisions granting issuers or persons responsible for the prospectus some flexibility when applying these guidelines.

[8] http://www.afm.nl/~/media/Files/rapport/engels/report-alternative-financial-performance-indicators.ashx
[9] http://www.pwc.com/gx/en/audit-services/corporate-reporting/publications/investor-view/investor-survey-edition.jhtml
[10] Bassen and others (2012), Kapitalmarktorientierte Rechnungslegung KoR 2012, page 350
[11] Kutting and Heiden (2002), Steuern and Praxis StuP, pages 1085-1089
[12] Hitz and Jennings (2008), Kapitalmarktorientierte Rechnungslegung KoR, pages 236-445
[13] Fredericks and Miller (2004), Accounting Review : Elliott (2006), Accounting Review : Andersson and Hellman (2007) : European Accounting Review : Bastini and Kasperzak (2013) ; Zeitschrift fur betriebswirtschaftliche Forschung zfbf, pages 622-660

Q5: Do you agree with the suggested scope of the term 'APM' as used in the [draft] guidelines? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
51	14	7	23	3	3	1

51. Split views were expressed on this question. 17 respondents including all user representatives and the SMSG concurred with ESMA that the definition of APM should be broad enough to include all measures necessary for a good understanding of an issuer's activity.

52. Thirty other respondents considered that the suggested scope of APMs was too wide, likely to cover almost every performance indicator and to capture financial information not always considered to be an APM. Eight respondents did not provide further comments besides agree/disagree.

53. Mixed views were also expressed on the measures that should be included within the scope of the term 'APM'. Some respondents thought that a difference should be made between APMs presented in the primary financial statements and other APMs derived from line items of financial statements presented elsewhere. Others believed that the definition of APMs should only focus on measures that are derived from financial statements prepared under the applicable financial reporting framework or those that include components that derive from financial statements regardless where they are presented.

54. Most auditors and three other respondents did not agree with the application of the proposed definition to certain business performance measures, such as sales per square meter or sustainability metrics of the activity of an issuer's business, as they considered it would be difficult to reconcile GAAP items with those measures. In this respect, they recommended that further guidance should be given on the situation when reconciliations are not possible.

55. Another respondent and the SMSG pointed out to the need of clearly distinguishing APMs defined by issuers on their own initiative from measures defined by the applicable financial reporting framework. They suggested to label those measures presented as 'APMs' in order to avoid possible confusion from users.

56. **ESMA's response:** ESMA took the approach that a robust definition of an APM would be achieved by covering all types of possible APMs rather than providing an exhaustive list. Therefore, ESMA believes that the scope of the term 'APM' should be broad enough to cover most of the measures not defined in the financial reporting framework. In that respect, ESMA took note of the issues concerning the labelling of APMs and included paragraph 22 into the final guidelines to explain the principle.

57. In response to the concerns expressed on the definition of an APM, ESMA has clarified the specific interaction between the final guidelines and the information required by other pieces of legislation in paragraph 4 of the final guidelines. It also amended the scope of the term 'APM' in paragraph 17 of the final guidelines by excluding non-financial information and by adding examples of information that should not be considered as 'APMs' for the purpose of these guidelines. These narrow the scope of the application of the proposed guidelines contributing significantly to the understanding of the term APM.

Q6: Do you believe that issuers should disclose in an appendix to the publication a list giving definitions of all APMs used? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
40	11	6	19	3	0	1

58. The majority of respondents, including user representatives and the SMSG, were supportive of the requirement to disclose the definitions of APMs used and the respective basis of calculation as they considered it would be helpful for readers of financial information. However, some of those respondents were concerned with the format of such publication and with the proposed form of the disclosures limited solely to an appendix. They feared it might create an overload of information with lengthy and complex clarifications. In cases where the definition or basis of calculation is straightforward, they were of the view that no detailed disclosures should be necessary.

59. Respondents representing preparers and auditors suggested leaving the choice of disclosure of the APM definitions to issuers, who will decide on the best way to present definitions and calculations. Respondents proposed as an alternative to include those definitions in the latest annual report, on the website of the issuer, in the notes to the financial statements or in other relevant documents that could be referred to.

60. **ESMA's response:** ESMA shares the view of user representatives and the SMSG that the definition of the measures used as well as their assumptions and basis for calculations should be clearly disclosed. It also takes note of the concerns expressed and is aware that an appendix may create unnecessary burden while its format could be subject to interpretation.

61. Therefore, instead of prescribing how issuers or persons responsible for the prospectus should provide the list of definitions, ESMA amended the proposed guidelines allowing issuers to find the best approach to provide that information to users. To avoid repetitions, issuers may use the practical expedient provided in the

final guidelines and include in the documents containing regulated information a reference (on the form of direct hyperlinks) where the list of definitions can be read.

Q7: Do you agree that issuers should disclose a reconciliation of an APM to the most relevant amount presented in the financial statements? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
42	11	7	18	3	2	1

62. Most respondents including user representatives agreed that issuers should present a reconciliation of APMs to the most relevant amount in the financial statements. Some respondents considered that the requirement to reconcile APMs to the relevant amounts in the financial statements should be practical for issuers and understandable for users of financial information. Some users suggested adding to the reconciliation the reasons why the issuer removed or added a reconciling item to the APM.

63. Six respondents believed that issuers should not always provide reconciliations as it would be burdensome without providing significant benefits to users. Some of them suggested to present a reconciliation only in the first document issued and subsequently refer to that first publication. Furthermore, those respondents believed that requirement on reconciliation should allow a suitable level of aggregation of the reconciled items to avoid excess complexity and practical challenges in financial statements and other issued documents.

64. Although the SMSG agreed with the principle of requiring reconciliation in most of the cases, it expressed doubts on the necessity to provide it in every single case. The SMSG believed that possible waivers on the reconciliation requirement could be granted when those reconciliations would not provide any added value.

65. The SMSG recalled the conclusions of the IFRS 8 post-implementation review which was addressed in the response to question 6 and made reference to an academic study[14] related to non-GAAP measures on the need for reconciliation. Researchers identified that high quality disclosure of the reconciliation of non-GAAP earnings to GAAP earnings reduces the mispricing of non-GAAP earnings. They concluded that investors are in a better position to value a company when APMs are directly readable from the financial statements.

[14] Zhang H. & L. Zheng (2011) The valuation impact of reconciling pro forma earnings to GAAP earnings, Journal of Accounting and Economics, 51, 186-202.

66. **ESMA's response:** ESMA highlights the importance of reconciliation and takes note of the respondents' agreement to require reconciliation between APMs and the most directly reconcilable line item, subtotal or total presented in the financial statements. Where financial statements are not yet published or not going to be published, APMs should be reconciled to the most directly relevant item which would be included in those financial statements if and when they will be published. Moreover, following the comments received, ESMA added in paragraph 29 of the final guidelines a waiver of the requirements to provide reconciliation if the APMs or its items are directly identifiable from the financial statements.

67. ESMA expects that issuers or persons responsible for the prospectus will present reconciliations in a way that will enable users to understand the items that were added or extracted from the figures in the financial statements. Considering the feedback received and the practicability of the issues raised, ESMA decided to provide some flexibility in the approach to be followed by issuers or persons responsible for the prospectus. Therefore, in order to avoid the disclosure overload and unnecessary burden to issuers or persons responsible for the prospectus when preparing the disclosures, ESMA has adjusted the provision on the reconciliation to require the disclosure of only material items instead of each item as stated in the CP. In addition, the practical expedient on the incorporation per reference is also allowed when providing reconciliations.

Q8: Do you agree that issuers should explain the use of APMs? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
37	12	8	13	3	0	1

68. Most respondents including the SMSG agreed that issuers should provide adequate information on the use of APMs and explain the reasons for considering them as a relevant depiction of the financial performance and operations of a business. They also believed that these explanations would help investors to analyse and value a business.

69. User representatives supported the inclusion of the reasons for the use of APMs, as they believed too often issuers make adjustments without explaining their reasoning. In their view, issuers should explain why they consider a particular APM more relevant than the IFRS figure.

70. However, 13 respondents (10 preparers and 3 accounting bodies and auditors) partially disagreed and considered that ESMA's requirement to permanently explain the use of APMs (paragraph 26 of the proposed guidelines) was 'inflexible', unnecessary and over-prescriptive. In their views, some APMs have a self-

explanatory purpose and others may be frequently used by specific industry. As users have a general understanding of the issuers' industry, a too extensive requirement is likely to lead to 'pointless boilerplate'.

71. Other respondents suggested that judgment should be allowed to issuers in determining the level of description and not increasing communication with boiler-plate information. They suggested less explanation of measures widely understood and used in the sector/market while providing more information when an APM was specific to an entity or less commonly used in the sector/market.

72. **ESMA's response:** ESMA shares the view of respondents that issuers should provide relevant information on the use of APMs and takes note of the issues raised. ESMA continues to believe that explanations about the use of a specific measure and its relevance to the decision making process are extremely useful for users when they analyse the performance of an issuer from the eyes of the management and enable them to take more informed decisions.

73. For this reason, ESMA expects that issuers or persons responsible for the prospectus, when making available this information, will not use boiler-plate language and will provide relevant information to help a correct understanding, comprehensibility or financial literacy of their investors and general public. ESMA believes that issuers or persons responsible for the prospectus will more likely obtain financing for their activity as users will better understand the fundamentals of their businesses and compare them with their competitors.

74. With respect to the concerns expressed by respondents, ESMA also reminds issuers or persons responsible for the prospectus that the APMs guidelines should not be applied to measures that are determined by law or regulations, thus where a specific sector measure is required by national law no explanations are required to be provided.

Q9: Do you agree that APMs presented outside financial statements should be displayed with less prominence, emphasis or authority than measures directly stemming from financial statements prepared in accordance with the applicable financial reporting framework? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
50	13	7	22	3	4	1

75. Overall, respondents disagreed that APMs presented outside financial statements should be displayed with less prominence that measures stemming from financial statements.

76. Only seven respondents including three user representatives and the SMSG agreed with ESMA's requirement to display APMs presented outside financial statements with 'less prominence' than measures derived from financial statements. The SMSG believes that, despite the location of APMs, whenever APMs are used to reflect past performance, they should always stem from financial statements prepared in accordance with the applicable financial reporting framework and reflect audited figures.

77. All but those seven respondents expressed concerns on the concept of 'less prominence'. They considered that APMs are usually used to facilitate users' understandability of the entity's financial performance, results of operations, and/or cash flows of the business and might therefore be relevant to that analysis. In their views, APMs should not be more prominent than measures reported in accordance with the applicable financial reporting measures, but should be enabled to be displayed with 'equal' prominence, emphasis or authority relative to the measures stemming from financial statements.

78. Two respondents considered that the current version of IAS 1 is not very exhaustive on defined measures. They noted that the recent amendments to this standard propose that additional sub-totals should not be displayed with more prominence than the subtotals specified in IFRS. Those respondents considered that the proposed guidelines may preclude issuers from presenting APMs, which in their view should not occur as these measures may be useful to the users of financial statements. Hence they believe that this requirement should be aligned with the IASB's amendment on this matter.

79. Two respondents drew ESMA's attention to comparable US SEC rules on the publication of non-GAAP measures and recalled that the SEC has taken a more flexible approach by only requiring to present non-GAAP measures with 'no greater' prominence than equivalent GAAP measures. In that respect, these respondents feared that ESMA's proposed guidelines would bring about a comparative disadvantage for European issuers.

80. Finally, the SMSG and some other respondents considered that the concept of prominence should be better explained and that ESMA should provide guidance on how to apply this concept in the context of the proposed guidelines.

81. **ESMA's response:** ESMA also acknowledges the importance of APMs for users to obtain a better understanding of the financial information provided by issuers or persons responsible for the prospectus. It is not the intention of ESMA to discourage issuers or persons responsible for the prospectus to provide this information. However, ESMA remains confident that figures stemming financial statements prepared in accordance with the applicable accounting framework are of primary relevance for users when assessing the performance of issuers.

82. In order to align this concept with other regulations issued by other regulators and to address the criticism raised by respondents, ESMA decided to amend the proposed guidelines enabling issuers or persons responsible for the prospectus to present

APMs with equal prominence compared to the figures/measures in the financial statements.

83. To avoid different definitions, interpretations and applications of the same principle between the IFRS and these guidelines, ESMA believes that the concept of prominence in these guidelines should follow the same principles on prominence set out by the IASB even if APMs are derived from other GAAPs.

Q10: Do you agree that issuers should explain the reasons for changing the definition and/or calculation of an APM? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
38	11	6	16	3	1	1

84. All respondents, including all user representatives and the SMSG, agreed that APMs should be used in a consistent and understandable way over time and thus issuers should explain the reasons for changing the definition and/or calculation of an APM.

85. As a principle, issuers should try to minimize changes to APMs so that the definition and calculation of APMs remain consistent and meaningful over time. However, some respondents pointed out that definitions may change over time as business activity evolves. In such cases, they agreed with ESMA that issuers should explain why newly defined APMs provide better information on the performance of the issuer, present the reasons for changing the definition and/or calculation of the APM, as well as appropriate comparatives.

86. **ESMA's response:** ESMA welcomes the support for meaningful and relevant explanations of the APMs used. For the sake of clarity, ESMA merged paragraphs 34, 35 and 36 of the proposed guidelines to reinforce the principles contained therein on the consistency of the use of those measures.

87. In order to provide users with an understanding of the changes that have occurred issuers or persons responsible for the prospectus should identify APMs that were modified in comparison with previous publications, such as labelling them differently or highlighting that their definition has been changed.

Q11: Do you believe that issuers should provide comparatives and / or restatements when an APM changes? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
35	10	5	16	3	0	1

88. Most respondents, including all user representatives and the SMSG, believed that issuers should use APMs in a consistent manner over time and not change them frequently. Furthermore, they agreed that in order to make meaningful comparisons of an issuer's performance over time, issuers should provide comparatives and/or restatements when an APM changes.

89. Only two respondents representing preparers disagreed with the provision of comparatives or restatements as they believed the proposed approach would be too onerous and that APMs were only changed if they have proven to be unhelpful to investors.

90. **ESMA's response:** ESMA welcomes the agreement on the principles included in the proposed guidelines on comparatives and restatements when APMs change in order to foster comparability of APMs with meaningful and relevant information when APMs are modified.

Q12: Do you believe that issuers should provide explanations when they no longer use an APM? If not, why?

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
34	10	5	15	3	0	1

91. Most respondents, including user representatives and the SMSG, agreed that issuers should provide explanations when they no longer use an APM. They recalled the importance of consistency and credibility of reported information in improving confidence towards issuers' financial communication.

92. Seven respondents representing accounting bodies and auditors pointed out that a request to report the reasons for changing the APMs would enable users to assess management's views and to eliminate concerns relating to management bias and 'cherry picking' of favourable APMs.

93. Nine respondents (representing accounting bodies and preparers) considered that the provision of additional explanation when an issuer no longer uses an APM should not be compulsory as it risks generating boilerplate disclosure and prevent issuers from exercising their judgment for changing a practice. In their views, issuers may stop using an APM because it is no longer important. Thus, it would be inappropriate to require disclosures about measures that are not presented anymore as there is no potential danger of misleading information.

94. **ESMA's response:** ESMA strongly believes that APMs should be consistently used over time and therefore maintains the provision for issuers to provide relevant explanations when they no longer use an APM. However, ESMA emphasises that the objective of the guideline is not to prevent changes to APMs, but rather to enable users to understand those changes, when they occur.

Q13: Do you agree that the [draft] guidelines will improve transparency, neutrality and comparability on financial performance measures to users? If not, please provide suggestions.

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
45	12	6	21	3	2	1

95. Overall, respondents, including user representatives and the SMSG, believed that the proposed guidelines would improve transparency, enhance comparability between issuers and lead more easily to unbiased financial information in documents containing regulated information.

96. Representatives of accounting bodies, users and auditors suggested publishing best practices or illustrative examples for the disclosures required by the proposed guidelines in order to provide accurate and relevant information to users. In this respect, a reliable benchmarking analysis and an unbiased 'management interpretation' are two key areas that enhance the neutrality and comparability of the financial performance measures. They also believed that consistency and comparability could be further enhanced with the development of industry or sector-wide approaches with industry bodies or a global harmonization of approaches under the auspices of the International Organization of Securities Commissions (IOSCO).

97. Nine respondents representing preparers considered that the improvement in transparency will only be marginal, as the proposed guidelines will generate complexities for users and ultimately result in boilerplate disclosures with no effect on neutrality or comparability between issuers. As financial reports vary in frequency, form and length, financial information will be more cumbersome and confusing. A

possible way forward would be to allow certain disclosures to be included by way of referencing to other published documents or to the issuer's website.

98. **ESMA's response:** ESMA welcomes the support received from respondents that the proposed guidelines will improve transparency and comparability in Europe. When initiating the guidelines, ESMA took into consideration the approach of other securities regulators in order to ensure consistency at global level.

99. ESMA intends to undertake a follow up review of the application of these guidelines in the future. This will allow European enforcers to identify good practices at European level and report accordingly to the public.

100. ESMA took into consideration the comments received and amended the guidelines to allow referencing when applying the guidelines. ESMA believes that, by doing so, it addresses the issue of disclosure overload, lengthy publications and confusing messages.

Q14: Do you agree with the analysis of the cost and benefit impact of the [draft] guidelines? Please provide any evidence or data that would further inform the analysis of the likely cost and benefits impacts of the proposals.

Number of respondents	Accounting bodies and auditors	User representative bodies	Preparer representative bodies	Regulators and government bodies	Standard setters	SMSG
30	10	4	13	2	0	1

101. Mixed views were expressed by 25 respondents who specifically answered this question while 5 other respondents considered that they were unable to make an opinion on the analysis of the cost and benefit impact.

102. Thirteen respondents (representing accounting bodies, auditors and users), including the SMSG, agreed with ESMA's analysis and believed that the benefits will be higher than the costs.

103. The SMSG considered that the additional cost for issuers would be marginal or even inexistent. In their view, issuers only make use of APMs on a voluntary basis when the benefits outweigh the related costs. As such, they believed that the costs that may be incurred by issuers when complying with the proposed guidelines should be connected to the use of APMs themselves rather than to the provision of providing disclosures on definitions or explanations, which does not imply a material cost. The SMSG also recognized that European enforcers will incur some additional costs which seemed to be necessary.

104. However, 12 respondents, mainly representing preparers, were more cautious and believed the cost analysis provided in the CP could be improved. They

considered there was a lack of identified benefits or evidence of problems and feared that the proposed guidelines would increase compliance and administrative burden to issuers with no sufficient benefit to investors to outweigh the cost to issuers. Finally, preparers considered that an increase in the volume of annual reports was likely to create an unnecessary flood of information for users and to reinforce the cost of information overload.

105. **ESMA's response:** ESMA takes note of the comments received and concurs with the users representatives' views that benefits will be generated by the implementation of the guidelines and the provision of relevant information on the use of APMs to better understand the fundamentals of an issuer and to help investors take well-informed decisions.

106. ESMA believes that the revised scope (excluding financial statements) and changes made to the guidelines in other areas (e.g. approach to reconciliations and the ability to reference), provide a more pragmatic and practical set of guidelines for issuers or persons responsible for the prospectus to comply with. ESMA expects that the changes made will decrease the burden for issuers or persons responsible for the prospectus.

107. Furthermore, ESMA is aware that quantifying benefits is a challenging exercise and sought the input from stakeholders in its CP. However, no respondent provided quantifiable input on this question. ESMA understands that all relevant stakeholders, issuers or persons responsible for the prospectus may face one-off costs with the initial implementation of guidelines. However, the expected benefits from the implementation of the guidelines are expected to outweigh the costs in the medium and long term

108. In this context, and as mentioned in the CP, ESMA remains confident that the improvement of disclosures resulting from the application of these guidelines will reduce the cost of capital, as the increase of transparency of information leads to more efficient capital allocation due to a better assessment of risks and pricing.

3 Annexes

3.1 Annex I - List of respondents

1	**ESMA Securities and Markets Stakeholders Group**
	Accounting bodies and auditors
2	Association of Italian audit firms (ASSIREVI)
3	Chartered Accountants Ireland
4	Compagnie Nationale des Commissaires aux comptes (CNCC)
5	Deloitte
6	Federation of European Accountants (FEE)
7	Finnish Institute of Authorized Public Accountants
8	FSR - Danske Revisorer
9	Grant Thornton
10	Institute of Chartered Accountants of Scotland (ICAS)
11	Institute for the Accountancy Profession in Sweden (FAR)
12	Institute of Chartered Accountants of England and Wales (ICAEW)
13	International Federation of Accountants (IFAC)
14	KPMG
15	Mazars
16	Price Waterhouse Coopers
17	one confidential
	Users representative bodies
18	CFA Society United Kingdom
19	Corporate Reporting Users' Forum
20	Danish Shareholder Association
21	Eumedion
22	Hungarian Compliance Professionals Working Group
23	French Society of Financial Analysts (SFAF)
24	Standard & Poor's Ratings Services
25	World Intellectual Capital Initiative
26	one confidential
	Preparers/ Issuers representative bodies
27	Acteo/ Medef
28	Association of British Insurers (ABI)
29	Association of Investment Companies (AIC)
30	Business Europe
31	Confederation of Danish Industry
32	Danish Bankers Association (DBA)
33	Deutsches Aktienintitut
34	Deutsche Bank

35	EuropeanIssuers
36	French Association of Large Companies (AFEP)
37	GC100
38	German Banking Industry Committee
39	German Insurance Association (GDV)
40	GlaxoSmithKline
41	Investment Management Association (IMA)
42	Insurance Europe
43	London Stock Exchange Group
44	Portuguese Banking Association (APB)
45	Quoted Companies Alliance
46	Rio Tinto
47	SAP
48	SBM Offshore
49	Stagecoach Group
50	Swedish Bankers' Association
51	Swedish Enterprise Accounting Group
52	The 100 Group
53	The Linde Group
54	UCB
55	One confidential
	Regulators and Government bodies
56	Financial Reporting Council (FRC)
57	Irish Auditing and Accounting Supervisory Authority (IAASA)
58	SIX Exchange Regulation
	Standard Setters
59	Accounting Standards Committee of Germany (ASCG)
60	Autorite des Normes Comptables (ANC)
61	European Financial Reporting Advisory Group (EFRAG)
62	Swedish Financial Reporting Board

3.2 Annex II - Cost-benefit analysis

1. Introduction

1. Pursuant to Article 16 of the ESMA Regulation, ESMA is empowered to issue guidelines addressed to CAs and/or financial market participants with a view to establishing consistent, efficient and effective supervisory practices within the European System of Financial Supervision, and to ensure the common, uniform and consistent application of Union law. The same article obliges ESMA to conduct open public consultations regarding guidelines to analyse the related potential costs and benefits, where appropriate. Such consultations and analyses shall be proportionate in relation to the scope, nature and impact of the guidelines.

2. Procedural issues and consultation process

2. In February 2014, ESMA has published the Consultation Paper on the Alternative performance Measures (CP on APMs or CP). In this CP, ESMA included a Cost and benefit analysis (CBA) assessing the expected costs and benefits that would be incurred or obtained by issuers or persons responsible for the prospectus, users and CAs with the application of the proposed guidelines.

3. When preparing this CBA, ESMA sought quantitative input that could enable ESMA to better assess whether the approach followed and the requirements included in the guidelines where proportional to the expected efforts required from issuers or persons responsible for the prospectus, users and CAs. However, the information required to perform this assessment is not publicly available and ESMA could not estimate quantitatively the costs and benefits without incurring into significant costs.

4. Information about the costs estimated for issuers or persons responsible for the prospectus to produce the information required by these guidelines (preparing the reconciliations, disclosing definitions and explanations of the measures used, providing comparatives and restatements, as well as changing the reporting systems) may vary significantly depending on the size of the financial market participant, the number of APMs used, the number of documents published, as well as the reporting systems currently used by issuers or persons responsible for the prospectus and users to produce and analyse this information.

5. Consequently, when preparing the CP, ESMA performed a qualitative assessment which was included in the CP and sought input on the quantitative assessment from issuers or persons responsible for the prospectus who were in a better position to provide ESMA with this information.

6. The CP included a question on the CBA asking financial market participants on (i) whether they agreed with the CBA included in the CP and (ii) quantitative information on the costs and benefits that would enable ESMA to better assess the impact that these proposals would have in the market.

7. When responding to the question, mixed views were expressed by 25 respondents who specifically answered this question while 5 other respondents considered that they were unable to give an opinion on the analysis of the cost and benefit impact.

8. Thirteen respondents (representing accounting bodies, auditors and users), including the SMSG, agreed with ESMA's analysis and believed that the benefits will be higher than the costs.

9. The SMSG considered that the additional cost for issuers would be marginal or even nil. In their view, issuers or persons responsible for the prospectus make use of APMs on a voluntary basis only when the benefits outweigh the related costs. As such, they believed that the costs that may be incurred by issuers or persons responsible for the prospectus when complying with the proposed guidelines should be connected to the use of APMs itself rather than to the provision of disclosures on definitions or explanations, which does not imply a material cost. The SMSG also recognised that CAs will incur some additional costs which seem to be necessary when monitoring the application of the guidelines by issuers or persons responsible for the prospectus.

10. Twelve respondents, mainly representing preparers, were more cautious and believed the cost analysis provided in the CP could be improved. They considered there was a lack of identified benefits or evidence of problems and feared that the proposed guidelines would increase compliance and administrative burden to issuers with no sufficient benefit to investors to outweigh the costs incurred by issuers. Finally, preparers considered that an increase in the volume of annual reports was likely to create an unnecessary flood of information for users and lead to an increase of the cost of analysing all the information provided by issuers.

11. ESMA took notes of the comments received and concurs with the users representatives' views that the benefits that will be generated with the implementation of the guidelines will offset the costs incurred. In this respect, ESMA expects that relevant information on the use of APMs to better understand why issuers or persons responsible for the prospectus use certain measures or performance indicators will be provided and such information will help investors to take well-informed decisions.

12. Furthermore, before the CP was published ESMA was aware that quantifying costs and benefits was a challenging exercise considering that there is no available information and thus sought the input from stakeholders in its CP. However, respondents did not provide any quantifiable input.

13. ESMA is aware that issuers or persons responsible for the prospectus will incur costs related to the application of these guidelines and expects that most of these costs will be one-off costs with the initial implementation of guidelines. However, as expressed by users and the SMSG, ESMA continues to believe that the expected benefits from the implementation of the guidelines are expected to outweigh the costs in the medium and long term for issuers or persons responsible for the prospectus and users.

14. In order to address the criticism received from respondents, ESMA has revised the scope (excluding financial statements) and changed the guidelines in other areas providing reliefs to reconciliations, appendix of definitions, and allowed issuers to reference to other documents to avoid repetitions and the overload of disclosures expressed by financial market participants.

15. The changes made to guidelines provide a more pragmatic and practical set of requirements for issuers or persons responsible for the prospectus to comply with, ESMA considers that the changes made will decrease significantly the burden that respondents estimated with the proposed guidelines without jeopardising the expected benefits for all the stakeholders affected.

16. Based on this assumption, ESMA considers that the information gathered and changes made do not require changes in the qualitative assessment done when the CP was published.

Application to prospectus

17. The consultation paper had a question whether prospectuses should be included in the scope of the guidelines. As mentioned in the Final Report, the majority of the respondents (including the SMSG) believed that prospectuses should be included in the scope, provided that some exceptions were made to take into account the specificities of the prospectus regime. Those respondents believed that a consistent and harmonised approach should be taken in relation to APMs regardless of where these measures are disclosed (e.g. management reports, prospectuses or disclosures made by issuers or persons responsible for the prospectus in light of the market abuse requirements).

18. Taking into account this support, and having discussed this issue with CAs in charge of the approval of prospectuses, the scope of the final guidelines was extended to include prospectuses and the final guidelines were amended to address the specificities of the prospectus regime. ESMA is aware that this extension of the scope will have an impact on the market stakeholders who are required to draw up a prospectus to raise capital, issue debt or derivatives or admit securities to trading on regulated markets.

19. ESMA considers that the impact of complying with the guidelines when drawing up a prospectus is not likely to be significant as explained in section 6 of this CBA.

3. Problem Definition

20. Issuers or persons responsible for the prospectus often publish financial data which are not defined by the applicable financial reporting framework as part of their financial statements, press releases, management reports, analyst's presentations, prospectuses and other documents. These financial data, named APMs for the purpose of the guidelines are frequently used by issuers or persons responsible for the prospectus to provide users with a better understanding of the performance, the

drivers of the business or the effects of external influences over the activity of an issuer or person responsible for the prospectus.

21. Over the years, divergent practices could be observed in relation to the presentation of APMs in issuers or persons responsible for the prospectus' public documents. It is ESMA's view that in some circumstances users may not understand the information provided or its relevance.

22. In some cases, APMs cannot be easily derived from or reconciled back to financial statements, which should constitute the most relevant information to be considered by users in making informed decisions. In other cases, APMs are described in terms which are not defined by issuers or persons responsible for the prospectus or by the applicable financial reporting framework and, consequently cannot be easily understood by users. Even where terms are defined, issuers or persons responsible for the prospectus can often be seen to depart from those definitions rendering the measure concerned difficult to contextualise.

23. Over and above, APMs also appear to be used by some issuers or persons responsible for the prospectus to present a confusing or optimistic picture of their performance to users by removing certain negative aspects. APMs can be misleading if they are inconsistently calculated or presented.

24. Taking into account the above mentioned facts, ESMA considered the need to issue guidelines to improve the presentation of APMs in order to ensure that users of financial information are provided with relevant and appropriate information.

4. Objectives of the guidelines

25. The guidelines are aimed at promoting the publication of transparent, neutral and comparable information of financial performance to users. These guidelines should contribute to the creation of a level playing field and the reduction in information asymmetry among users and increase market confidence in financial information that is provided to the public.

26. It is the objective of these guidelines to increase the level of disclosures on APMs so that users are enabled to better understand the financial data that is provided by issuers or persons responsible for the prospectus with regards to their performance.

5. Policy options

27. In order to address the problem and comply with the objectives identified above, ESMA has considered the possibility of no ESMA action. However, taking into consideration the CESR Recommendation and the problems identified above that continue to be observed, ESMA believes that keeping the status quo should be disregarded. In addition, considering the past experience obtained with the implementation of CESR Recommendation, ESMA does not believe that this problem will be solved by market forces and competition environment among issuers or persons responsible for the prospectus.

28. Furthermore, ESMA also believes that the overall costs do not outweigh benefits, and therefore a regulatory action on this subject is justified. ESMA is of the opinion that issuing guidelines is the best solution to improve market confidence with low costs to issuers or persons responsible for the prospectus and CAs.

6. The likely economic impacts

29. The implementation of these guidelines on APMs should bring benefits to users and issuers or persons responsible for the prospectus; however, it will probably introduce some additional costs. ESMA has analysed the costs and benefits of the application of these guidelines and concluded that applying these guidelines will affect issuers or persons responsible for the prospectus, users and CAs as described below.

Issuers or persons responsible for the prospectus

Benefits

30. The application of these guidelines will improve the communication with users by increasing the understandability, relevance and comparability of the APMs provided. Supplementing public documents containing regulated information, with the disclosure principles set out in these guidelines will enhance the transparency of APMs used in documents containing regulated information that are made available to the public. Moreover, it will reduce the asymmetry of information between users particularly between capital owners and management, which may lead to increased users' confidence since they will be able to evaluate more effectively issuers or persons responsible for the prospectus' performance.

31. ESMA expects that the compliance with the guidelines will increase the transparency and comprehensibility of APMs included by issuers or persons responsible for the prospectus in regulated information documents or prospectuses. In the long term, ESMA also believes that the improvement of disclosures resulting from the application of these guidelines will reduce the cost of capital, as the increase of transparency of information normally leads to more efficient capital allocation due to a better assessment of risks and better pricing.

Costs of compliance in documents containing regulated information

32. The application of these guidelines will only affect issuers or persons responsible for the prospectus that disclose APMs in documents containing regulated information that are made available to the public. The costs associated with the implementation of these guidelines may increase depending on the number of APMs reported.

33. Issuers or persons responsible for prospectus will most likely incur both one-off costs (implementation costs) and ongoing costs.

(i) One-off costs (costs of implementation)

34. Issuers or persons responsible for the prospectus may incur costs with the implementation of these guidelines such as adaptation of the financial reporting system and reporting procedures. However, such costs should be mitigated on the basis that:

   i. some disclosure principles were already included in the CESR Recommendations (on prospectuses or financial information disclosed under TD)[15], and therefore some issuers or persons responsible for the prospectus already put them in place;

   ii. the disclosure principles were not included in the CESR Recommendations (on prospectuses or financial information disclosed under TD) or were not complied with by issuers or persons responsible for the prospectus require information that is already available to the financial market participant.

35. ESMA is of the view that, when an issuer or persons responsible for the prospectus decide to disclose an APM, it has already collected information regarding the components of that APM, has an easy access to historical information that allows them to provide comparatives and already acknowledges its relevance to users.

36. Therefore, ESMA is of the opinion that the costs related to the implementation of these guidelines will not be significant.

(ii) Ongoing costs

37. As previously mentioned, ESMA believes that most of the information required by these guidelines is already collected for internal management purposes. However, ESMA acknowledges that data gathered for management purposes may not be in the format needed to satisfy the disclosure principles set out in these guidelines which may result in ongoing costs.

38. ESMA is of the view that these costs will not be significant because APMs should generally not change over periods. Therefore, ongoing costs will relate almost exclusively to updating information for every reporting period which will be limited once the reporting system and reporting procedures are in place.

Users

Benefits

39. ESMA is of the view that the application of these guidelines will improve the understandability, relevance and comparability of APMs provided in documents containing regulated information or prospectuses that are made available to public by issuers or persons responsible for the prospectus.

[15] CESR Recommendation on Alternative Performance Measures and ESMA update of the CESR recommendations (ESMA/2013/319)

40. Users will be able to understand the link between the financial statements prepared under the applicable financial reporting framework, which in the case of annual financial statements are audited, and the performance measures used by management. The reconciliations required in these guidelines will provide an increased level of assurance on the quantitative information communicated through APMs.

41. Moreover, these guidelines will allow users to understand the relevance of each APM in the management decision process. Therefore, the qualitative disclosures required on the relevance of each measure will permit users to choose those APMs which are of most relevance for their investment decisions.

42. Similarly, full disclosure of all components of APMs used will enable users to understand the adjustments done by management to figures presented in the financial statements. ESMA is of the opinion that this information will help users to make better grounded projections and estimates of future cash flows and assist them in performing equity analysis and valuations.

43. It is also expected that the application of the guidelines will contribute to enhancing the comparability and consistency in the use of APMs. Users will be able to understand the changes in APMs' components, the reasons for these changes and their relevance.

44. These disclosures will allow users to compare information between periods and will help them in comparing the performance of issuers in the same sector or market.

45. Finally, ESMA also believes that these guidelines may also help users in evaluating management performance more effectively.

Costs

46. The information provided by issuers or persons responsible for the prospectus in complying with these guidelines will increase the level of disclosures in the documents made available to the market with the potential effect of increasing the time spent by users in analysing the information provided.

47. On the other hand, the application of these guidelines may lead issuers or persons responsible for the prospectus to provide more qualitative information in order to avoid providing disclosures on quantitative measures. This situation might have a negative effect on the understandability of the information disclosed and it can potentially impair their access to quantitative information that may be useful to make their investment decisions. Nevertheless, ESMA believes that this situation is unlikely to occur since APMs have been widely used over time and competition between issuers or persons responsible for the prospectus together with users' demands for this information will prevent this situation from occurring.

48. ESMA considers that the impact of complying with the guidelines when drawing up a prospectus are likely to be reduced as the assessment of costs and benefits included above is also applicable to the entities drawing up a prospectus and/or responsible for drawing up prospectuses. In order to address the specificities of the prospectuses, the following paragraphs provide more detailed information on the specific impact of these guidelines on persons responsible for the prospectus drawing up a prospectus.

49. Notwithstanding what was previously before, it is expected that the changes proposed in the guidelines will have a higher impact when issuers or persons responsible for the prospectus drawing up a prospectus are not within the scope of the proposed guidelines, e.g. issuers without securities admitted to regulated markets. If issuers or persons responsible for the prospectus are already required to apply these guidelines because they are subject to the TD (and, by extension, the MAR) requirements, the costs of including this information in a prospectus should be low as the information provided in regulated information documents may be reused when drawing up a prospectus.

50. On the other hand, if issuers do not yet have securities admitted to trading but will have them in the future, such issuers drawing up a prospectus for admission to trading or Initial Public Offers (IPOs) subsequently admitted to regulated markets, the costs related to the application of these guidelines to prospectuses will be merely an anticipation of the costs that they will incur in the future when they are subject to the TD (and by extension MAR) provisions.

51. ESMA acknowledges that the Prospectus Directive is also applicable to public offers which may not be subsequently admitted to trading on the regulated markets. In those cases, those stakeholders would only apply these guidelines for the purpose of a prospectus's approval.

52. In this regard, ESMA notes that the principles included in the guidelines are in most situations consistent with the principles included in the ESMA update of the CESR recommendations (ESMA/2013/319), paragraphs 23-24 and 95-97, which issuers or persons responsible for the prospectus should already apply when drawing up a prospectus.

53. Finally, ESMA notes that the inclusion of APMs in prospectuses (as well as any other document containing regulated information) is voluntary as it is not required by the PD. Thus, entities drawing up prospectuses may always avoid incurring in any costs if they decide not to use/include APMs.

Competent Authorities (CAs)

Benefits

54. CAs will have to implement these guidelines as part of their supervisory activities. These guidelines provide CAs with a clear framework against which they can require

issuers or persons responsible for the prospectus to provide information regarding APMs disclosed in documents containing regulated information or prospectuses that are made available to public which are subject to their supervision. It is likely that CAs will be able to check more easily the completeness and the relevance of the information that should be provided by analysing the compliance to these guidelines instead of requiring individual information to each APM that is disclosed in documents containing regulated information that are made available to the public by issuers or persons responsible for the prospectus.

55. Therefore, the guidelines should help reducing the need for one-off and on-going requests for further guidance and clarification from users, and may reduce costs of supervision which are currently spent by CAs when addressing complaints from users in relation to the misunderstanding or misuse of APMs.

Costs

56. The guidelines may also lead to some additional costs to the extent that CAs will be required to incorporate them into their supervisory practices. This implies that CAs may need to provide training to existing staff or hire additional staff to analyse the compliance of these guidelines. However, it is also likely that costs related to complaints of users requiring this information will be reduced, as users will have more information regarding these APMs which will enable them to make their own assessment of the risks of their investments if all information required in these guidelines is provided.

3.3 Annex III - Opinion of the Securities and Markets Stakeholder Group

Position paper from the Securities and Markets Stakeholder Group

I. Background

1. In October 2005, the Committee of European Securities Regulators (CESR), ESMA's predecessor body, published a Recommendation on Alternative Performance Measures *("CESR Recommendation"* CESR/05-178b*).* The CESR Recommendation was issued mainly in order to reinforce the objectives of Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

2. Given the CESR Recommendation has now been in force for more than 8 years, ESMA has decided to review it with the objective of strengthening the principles contained in it. ESMA now plans to re-issue the principles as ESMA [draft] guidelines under Article 16 of the ESMA Regulation in relation to the acts referred to in Article 1(2) of the ESMA Regulation, which include the Transparency Directive, thus ensuring that issuers and Competent Authorities (CAs) will make every effort to comply with them.

3. At the SMSG meeting held on 29 January 2014, Roxana Damianov, ESMA, presented the main content of the draft ESMA Consultation Paper on Alternative Performance Measures, according to a presentation shared with the meeting, and informed that the consultation paper would go for approval to the next ESMA Board meeting and thereafter be opened for consultation. The SMSG Chair noted that SMSG would consider a working group on the topic once the consultation period had opened.

4. On 13 February 2014 the final version of the ESMA Consultation Paper on APM was published, with deadline for consultation set on 14 May 2014. ESMA issued this Consultation Paper (CP) to inform market participants about the background to its decision to revise the CESR Recommendation and seek their views on such revision.

5. On 12 March 2014 a Working Group on APM was formed with a task to prepare a discussion at the next SMSG meeting on 10 April, with a view to finalize the response before the deadline of 14 May 2014.

6. At the SMSG meeting held on 10 April 2014, a Discussion Note prepared by the Working Group was presented and discussed. There was a consensus that the final report should be prepared in line with the Discussion Note.

II. Response to the ESMA Consultation Paper

7. SMSG welcomes EMSA's initiative to imply a common approach to be adopted by CAs and issuers towards the use of APMs by issuing guidelines. The Transparency Directive does not request ESMA to issue respective guidelines. However, according to Art. 16 of the

Regulation 1095/2010, ESMA shall, with a view to establishing consistent, efficient and effective supervisory practices within the ESFS, and to ensuring the common, uniform and consistent application of Union law, issue guidelines addressed to competent authorities or financial market participants.

Q1: Do you agree that the ESMA [draft] guidelines should apply to all issuers defined as a legal entity governed by private or public law, other than Member States or Member State's regional or local authorities, whose securities are admitted to trading on a regulated market, the issuer being, in the case of depository receipts representing securities, the issuer of the securities represented regardless of the financial reporting framework they use to report? If not, why?

8. The ESMA [draft] guidelines are much more extensive than those specified in the CESR Recommendation that is currently in force. The CESR Recommendation applies to financial performance figures of listed companies focusing on issuers reporting under IFRS. “Listed companies” is generally under-stood as companies, whose shares are listed (admitted to trading) on a regulated market. The new guidelines will be applicable not only to those issuers, whose shares are listed on a regulated market, but also to issuers of other listed securities, including bonds and depository receipts. This is a right direction.

Q2: Do you agree that the ESMA [draft] guidelines should apply to APMs included in:

a) financial statements prepared in accordance with the applicable financial reporting framework, that are made publicly available, and

b) all other issued documents containing regulated information that are made publicly available?

If not, why?

9. Yes, APMs make sense either because they more effectively reflect the way the market values specific industries - based on multiples or other indicators that are not included in financial statements - or the measures management use to assess day to day performance. In both cases they ought to be included in all the documentation published by the company. If an APM makes sense it must be consistently used, so the guidelines should apply to it in any case.

Q3: Do you believe that the ESMA [draft] guidelines should also be applicable to prospectuses and other related documents, which include APMs (except for pro-forma information, profits forecasts or other measures which have specific requirements set out in the Prospectus Directive or Prospectus Directive implementing regulation)? Please provide your reasons.

10. The current CESR Recommendation explicitly excludes information contained in prospectuses published in accordance with EU legislation on prospectus, which was subject to another CESR recommendation. We strongly believe the new guidelines should also apply to APMs published in prospectuses and related documents. This is very important and helpful for investors, as they will be able to check the consistency of information (and

financial data) in prospectuses with information published later on in financial reports after the company becomes listed. There is no reason why prospectuses should be exempt from transparency requirements.

Q4: Do you believe that issuing ESMA guidelines constitute a useful tool for dealing with the issues encountered with the use of APMs? If not, why?

11. We believe the ESMA guidelines will be very useful for all market participants, however one comment is necessary. In paragraph 9 of the Consultation Paper we can read that *"the [draft] guidelines apply to NCAs and to issuers"*, but in paragraph 19 of the CP they are directed much broader, *"to NCAs and financial market participants"*, which includes not only issuers, but also several other groups of participants. We do understand this is consistent with art. 16(3) of the Regulation (EU) No 1095/2010 establishing ESMA, specifying that *"the competent authorities and financial market participants shall make every effort to comply with [ESMA] guidelines"* (*nb.* it is not cited exactly in paragraph 19, as "shall make" is replaced there with "must make"). However some inconsistency is visible here, so it should be clarified that the ESMA guidelines are directed to issuers only (who should apply them) and not to other financial market participants – they are only "users" of APMs provided by issuers.

Q5: Do you agree with the suggested scope of the term APM as used in the [draft] guide-lines? If not, why?

12. Yes, we agree with the suggested scope of the term APM as used in the proposed guidelines. A broad definition what APMs are in general is necessary, with the aim of clarifying the scope of the guide-lines. And within such a broad definition it should be the task of issuers only to define any specific APMs they want to use and publish.

13. However, we draw ESMA's attention on the fact that we don't exactly know what is really a non-IFRS measure. The IFRS do not really define a lot of items, but some items are customarily defined in a particular way. We can envision preparers using this argument to avoid providing any definitions.

Q6: Do you believe that issuers should disclose in an appendix to the publication a list giving definitions of all APMs used? If not, why?

14. Yes, we believe that issuers should disclose in an appendix to the "big" publication (like prospectus of annual report) a list giving definitions of all APMs used. Moreover, we encourage ESMA to require that issuers state clearly that they are adjusted measures.

15. Indeed, segment reporting under IFRS 8 allows the disclosure of non-IFRS measures inside the notes to financial statements, as long as these are defined. In practice, companies very seldom provide definitions for the items they use in the segment note. It is true that often they would use the same names for the line items as on the face of the financial statements, so the assumption is that they do not need to define them. However, the post-implementation review for IFRS 8 conducted by the IASB (final report published mid-2013) reveals that users would prefer that non-IFRS items be marked accordingly by having their name state clearly that they are adjusted measures (e.g., all names be preceded by the term "adjusted"). The IASB states it will consider this point as part of its disclosure framework work.

16. However a question arises whether all the APMs definitions should be repeated in every document or publication, as it could effect in some kind of overload of information and all the documents would have to be larger, creating additional and unnecessary cost to issuers. Therefore it seems that definitions should be fully enclosed in "big" documents only, but in other documents (like ongoing reports, press releases etc.) only an indication that the complete glossary is contained in the last annual report and/or at the company website could be enough. Also a link could be included to the full definition (e.g. to the issuer's website).

Q7: Do you agree that issuers should disclose a reconciliation of an APM to the most relevant amount presented in the financial statements? If not, why?

17. Yes, we agree that issuers should disclose a reconciliation of an APM to the most relevant amount presented in the financial statements. Nevertheless, we draw ESMA's attention on the fact that having regulations that ask for definitions and reconciliations does not necessarily mean that disclosure transparency automatically improves. Besides the non-compliance issue, it appears that practical application may be less straightforward than we think, and having that information does not mean it is also understandable.

18. On the one hand, from a standard-setting point of view, we know that IFRS 8 requires segment figures to be reconciled to group-level totals. In practice, the segment note does not even contain reconciliations, or these are very superficial. When reconciliations are provided, reading these tables is most of the time quite hard – they seem convoluted and are very hard to follow. The post-implementation review report confirms this opinion. More precisely, investors complain that reconciliations are not properly explained and are confusing, while preparers have mixed opinions about how easy it is to provide reconciliations and how clear the reconciliation requirements are. On the other hand, from an academic perspective, and specifically related to non-GAAP measures, Zhang and Zheng (2011) find that high quality reconciliation disclosures of non-GAAP earnings to GAAP earnings reduce the mispricing of non-GAAP earnings. Therefore, according to this same paper, it seems that well-done reconciliations indeed help investors value a company.

19. Furthermore, a question may arise whether reconciliations are necessary and useful in every single case. Therefore a differentiated approach for application and presentation of APMs taking into ac-count relevance and practicability might be applied, together with possibility of waiving the required reconciliations in cases where they would not build any added information value.

Q8: Do you agree that issuers should explain the use of APMs? If not, why?

20. Yes, we agree that issuers should explain the use of APMs.

21. However, it still remains several questions in relation to the disclosure overload issue. Doesn't a requirement for providing definitions for all non-GAAP items used in each document clutter the disclosure? If we think about firms' presentations to analysts and investors, they usually have a slide warning about the estimates behind forward-looking disclosures, but we doubt anyone ever reads this slide, it's just cluttering the presentation. Where should the definitions be? Each time the item is used and in each document? Should

the audience be taken into consideration? Maybe the financial analyst, who knows the firm very well, doesn't need to be reminded every time what one item stands for, and would in fact see this as an increase in the number of pages he needs to read.

Q9: Do you agree that APMs presented outside financial statements should be displayed with less prominence, emphasis or authority than measures directly stemming from financial statements prepared in accordance with the applicable financial reporting framework? If not, why?

22. Yes, we agree that APMs presented outside financial statement should be displayed with less prominence, emphasis or authority than measures directly stemming from financial statement prepared in accordance with the applicable financial reporting framework. Whenever APMs are used to the past performance, they should always stem from financial statements prepared in accordance with the applicable financial reporting framework and should reflect audited figures.

23. However, in our opinion, paragraphs 31 and 33 on page 13 of the Consultation Paper are not very clear – what does "the context of an APM" mean? What will be considered "greater prominence"? The literature on impression management that looks at press releases considers that the bullet points following the title are more prominent than the text that follows. But how can this be judged in presentations to analysts, for example? Of course, this assumes that impression management and investors' behavioral biases play a role.

Q10: Do you agree that issuers should explain the reasons for changing the definition and/or calculation of an APM? If not, why?

24. Yes, we agree that issuers should explain the reasons for changing the definition and/or calculation of an APM.

25. Nevertheless, we wonder how will the truthfulness of those reasons be checked and we think it's useless to require this if it cannot be reliably enforced. Therefore we would consider such information more trustworthy if provided voluntarily.

Q11: Do you believe that issuers should provide comparatives and/or restatements when an APM changes? If not, why?

26. Yes, we believe that issuers should provide comparatives and/or restatements when an APM changes. And we specifically encourage ESMA to be clearer on the number of years required to restate for comparative purposes.

27. Indeed, we know that issues related to providing comparative information in segment reporting arise when companies change their segmentation. Most companies' current practice is to not disclose any restated information beyond the prior year. As a response to the post-implementation review for IFRS 8, users claim such changes make the trend-line impossible to assess and have asked for as much as five years of restated data. The IASB is considering this as part of the work on the disclosure framework but thinks that restatements for the previous five years would be too costly for the preparers to produce.

28. Otherwise, in our opinion, comparability of non-GAAP measures between companies is very hard to achieve because each manager could be adjusting the measure in different ways – eventually what we could potentially compare is still the GAAP measure that the non-GAAP measure should be reconciled to. We think it's an open question whether users want to see the company through the management's eyes or whether they want to "put it in a box." Interestingly, the post-implementation review for IFRS 8 reveals that a large proportion of users would like to see the operating segments of the company from the manager's perspective, but have the segment line-items standardized (i.e., the standard should define the line-items to be disclosed in the segment note.) In this way, there would be at least some comparability between companies.

29. Last but not least, according to the IASB Conceptual Framework and the recent academic literature, we would like to underline that comparability refers to cross-sectional comparisons of companies (e.g., comparing two different companies), while consistency mainly refers to time-series comparisons for the same company (e.g., comparing across years). For clarity, there's also a distinction between comparability, consistency and comparative information. Providing comparative information means restating prior disclosures to provide information that is comparable with what is currently disclosed in order for users to be able to judge the trend.

Q12: Do you believe that issuers should provide explanations when they no longer use an APM? If not, why?

30. Yes, especially because in practice an issuer may decide to discard an APM when it no longer provides a positive picture of the company.

Q13: Do you agree that the [draft] guidelines will improve transparency, neutrality and comparability on financial performance measures to users? If not, please provide suggestions.

31. We fully agree with this, and the reasons are explained in the answers to all the previous questions.

Q14: Do you agree with the analysis of the cost and benefit impact of the [draft] guidelines? Please provide any evidence or data that would further inform the analysis of the likely cost and benefits impacts of the proposals.

32. It is difficult to find any special evidence or exact data, but we strongly believe the benefits will be much higher than costs. Of course there will be some additional costs for NCAs, but it seems to be necessary.

33. We all agree that the additional cost for issuers will be rather marginal (almost no cost at all), as costs may be connected with using some APM by issuers (on voluntary basis, if they want to use any APM), rather than with defining or describing them. It means: if the issuer uses an APM, he should understand it, so he should have his own definition of that APM. Adding that definition (and some explanation, if necessary) to the document where that APM is used, should be rather cheap. But issuers will use APMs only if they so wish, and if they think that the benefits will outweigh the related costs.

34. Another comment is that requirement to publish a description of APMs may have a negative effect on prospectuses and annual reports, as the number of pages in those documents may increase (however not so greatly), generating an additional 'cost' of reading for users. It may also create an unnecessary flood of information generated by additional (or longer) ongoing reports, not always necessary or important. However it should be taken into account that it is a decision of an issuer to use APMs, and if he wants to use them, he should explain them to the users, so users understand well what issuers are telling them.

References

- **CESR**: CESR Recommendation on Alternative Performance Measures, October 2005, Ref: CESR/05-178b

- **ESMA**: Consultation Paper. ESMA Guidelines on Alternative Performance Measures, 13 February 2014, ESMA/2014/175

- **Zhang H. & L. Zheng (2011),** The valuation impact of reconciling pro forma earnings to GAAP earnings, *Journal of Accounting and Economics*, 51, 186-202.

3.4 Annex IV - Guidelines on Alternative Performance Measures

I. Scope

Who?

1. These guidelines are addressed to:

   - issuers defined as natural persons or legal entities governed by private or public law, other than States, whose securities are admitted to trading on a regulated market and who are required to publish regulated information as defined by the TD.

     In the case of depository receipts admitted to trading on a regulated market, the issuer means the issuer of the securities represented, whether or not those securities are admitted to trading on a regulated market.

   - persons responsible for the prospectus under article 6 (1) of the Prospectus Directive.

2. These guidelines apply to all competent authorities (CAs) under the Transparency Directive or the Market Abuse Regulation or the Prospectus Directive.

What?

3. These guidelines apply in relation to APMs disclosed by issuers or persons responsible for the prospectus when publishing regulated information and prospectuses (and supplements). Examples of regulated information are management reports disclosed to the market in accordance with the Transparency Directive and disclosures issued under the requirements of article 17 of the Market Abuse Regulation, for example ad-hoc disclosures including financial earnings results.

4. By way of derogation from the aforementioned paragraph these guidelines do not apply to APMs:

   - disclosed in financial statements as defined in section II of these guidelines;

   - disclosed in accordance with applicable legislation, other than the applicable financial reporting framework[16], that sets out specific requirements governing the determination of such measures. Therefore, the guidelines do not apply to measures included in prospectuses such as pro forma financial information, related party transactions, profit forecasts, profit estimates, working capital statements and capitalisation and indebtedness for which the specific

[16] While these Guidelines do not apply to financial statements they do apply to other sections that make up the annual and half-yearly financial reports, in particular management reports or interim management reports as relevant.

requirements of the prospectus regime apply. Similarly, the guidelines should not be applicable to prudential measures including measures defined in the Capital Requirements Regulation and Directive – CRR/CRD IV.

When?

5. These guidelines apply to APMs disclosed by issuers or persons responsible for the prospectus when publishing regulated information or prospectuses on or after 3rd July 2016.

II. References and definitions

Legislative references

ESMA Regulation	Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC.
Market Abuse Regulation	Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation).
Transparency Directive	Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are traded on a regulated market and amending Directive 2001/34/EC[17].
Directive implementing the Transparency Directive	Directive 2007/14/EC, of 8 March 2007, laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market.
Prospectus Directive	Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading.

Abbreviations

APM	Alternative Performance Measure
EEA	European Economic Area
ESMA	European Securities and Markets Authority

[17] As last amended by Directive 2013/50/EU. Insofar as relevant, until the time for transposition of Directive 2013/50/EU has run out, references to the Transparency Directive shall be read in accordance with its provisions as in force before their amendment by Directive 2013/50/EU.

GAAP	Generally Accepted Accounting Principles
IASB	International Accounting Standards Board
IFRS	International Financial Reporting Standards
CAs	Competent Authorities

Definitions

Unless otherwise specified, terms used and defined in the Transparency, Prospectus and Market Abuse Directives have the same meaning in these guidelines. Some of the terms defined are recalled hereunder for the ease of reference. In addition, the following definitions apply:

Applicable financial reporting framework	For the purpose of these guidelines any of the following: (i) International Financial Reporting Standards (IFRS) as adopted in the EU pursuant to Regulation (EC) No 1606/2002 on the application of international accounting standards or (ii) the accounting requirements stemming from the transposition of the European Accounting Directives (78/660/EEC, and 83/349/EEC or 2013/34/EC) into the legal system of the Member States of the European Union or (iii) Generally Accepted Accounting Principles (GAAP) laying down equivalent requirements in accordance with Commission Regulation (EC) No 1569/2007 establishing a mechanism for the determination of equivalence of accounting standards applied by third country issuers of securities pursuant to Directive 2003/71/EC and 2004/109/EC of the European Parliament and of the Council for issuers that are exempted from the requirement of preparing IFRS as endorsed in the EU.
Financial statements	For the purposes of these guidelines, financial statements refer to annual, half-yearly financial statements and additional periodic financial information prepared in accordance with the applicable financial reporting framework and disclosed by issuers or persons responsible for the prospectus in accordance with the Transparency Directive or the Prospectus Directive.
Prospectus	For the purposes of these guidelines, prospectus refers to a document prepared in accordance with Directive 2003/71/EC.
Issuer	For the purpose of these guidelines an issuer is a natural person or a legal entity governed by private or public law, other than a State, whose securities are admitted to trading on a regulated market. In the case of depository receipts admitted to trading on a regulated market, the issuer means the issuer of the securities represented, whether or not those securities are admitted to trading on a regulated market.
Regulated information	All information which the issuer, or any other person who has applied for the admission of securities to trading on a regulated market without the issuer's consent, is required to disclose under

	the Transparency Directive, under Article 6 of the Market Abuse Directive, or under the laws, regulations or administrative provisions of a Member State adopted under Article 3(1) of the Transparency Directive (transposition of the Transparency Directive) [18].
Securities	Transferable securities as defined in Article 4(1), point 18, of Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments with the exception of money-market instruments, as defined in Article 4(1), point 19, of that Directive having a maturity of less than 12 months, for which national legislation may be applicable

III. Purpose

6. The guidelines are aimed at promoting the usefulness and transparency of APMs included in prospectuses or regulated information. Adherence to the guidelines will improve the comparability, reliability and/or comprehensibility of APMs. Issuers or persons responsible for the prospectus which comply with these guidelines will provide a faithful representation of the financial information disclosed to the market.

7. ESMA is of the view that issuers or persons responsible for the prospectus who decide to provide APMs should do so in a way that is appropriate and useful for users' decision-making. Within the scope of its powers as set out in the ESMA Regulation, ESMA may issue guidelines under Article 16 of the ESMA Regulation in relation to the acts referred to in Article 1(2) of the ESMA Regulation, which include the Transparency Directive, Market Abuse Directive and the Prospectus Directive.

8. Based on the Transparency Directive's objective of providing equivalent investor protection at EU level and the underlying principle of providing a true and fair view of an issuer's assets, liabilities, financial position and profit or loss pursued by the provisions, ESMA considers that a common approach to APMs is necessary to ensure consistent, efficient and effective supervisory practices and a uniform and consistent application of the Transparency Directive (and by extension the Market Abuse Directive).

9. In line with its aim of promoting protection of actual and potential investors, Article 5 of the Prospectus Directive sets out the principle that all information included in a prospectus shall be presented in an easily analysable and comprehensible form. ESMA is of the view that, where persons responsible for the prospectus decide to include APMs in a prospectus, this principle of comprehensibility dictates that such APMs should be defined, provided with meaningful labels and reconciled to financial statements and their relevance and reliability should be explained.

[18] As of 3 July 2016 references to Directive 2003/6/EC shall be construed as references to Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC and shall be read in accordance with the correlation table set out in Annex II of this Regulation.

10. On the basis of the above considerations, ESMA has decided to issue these guidelines. The guidelines set out a common approach towards the use of APMs and are expected to benefit users and to promote market confidence.

IV. Compliance and reporting obligations

Status of the guidelines

11. This document contains guidelines issued under Article 16 of the ESMA Regulation addressed to issuers or persons responsible for the prospectus and CAs. In accordance with Article 16(3) of the ESMA Regulation, CAs and issuers or persons responsible for the prospectus must make every effort to comply with guidelines.

12. For the avoidance of doubt, these guidelines do not displace any obligations to comply with requirements set out in Regulations or under Directives. Accordingly, the requirements in MAR relating to prompt disclosure of information to the market or the public as required under the applicable laws and regulations should be complied with.

13. CAs with responsibilities for supervising the TD and MAR requirements should incorporate these guidelines into their supervisory practices and monitor whether issuers comply with them.

14. CAs with responsibilities in approving prospectuses should incorporate these guidelines into their supervisory practices to ensure that persons responsible for the prospectus comply with them.

Reporting requirements

15. Competent authorities to which these guidelines apply must notify ESMA whether they comply or intend to comply with the guidelines, with reasons for non-compliance, within two months of the date of publication by ESMA to corporate.reporting@esma.europa.eu In the absence of a response by this deadline, competent authorities will be considered as non-compliant. A template for notifications is available from the ESMA website.

V. Guidelines on Alternative Performance Measures

16. These guidelines set out principles in bold with subsequent explanatory, elaborating and exemplifying paragraphs. In order to comply with these guidelines issuers or persons responsible for the prospectus have to comply with the guidelines as a whole.

What is an APM?

17. **For the purpose of these guidelines an APM is understood as a financial measure of historical or future financial performance, financial position, or cash flows, other than a financial measure defined or specified in the applicable financial reporting framework.**

18. APMs are usually derived from (or based on) the financial statements prepared in accordance with the applicable financial reporting framework, most of the time by adding or subtracting amounts from the figures presented in financial statements. Examples of APMs include: operating earnings, cash earnings, earnings before one-time charges, earnings before interest, taxes, depreciation and amortisation (EBITDA), net debt, autonomous growth or similar terms denoting adjustments to line items of statements of comprehensive income, statements of financial position or statements of cash flow.

19. In accordance with the definition in paragraph 17, these guidelines are not applicable to:

    - measures defined or specified by the applicable financial reporting framework such as revenue, profit or loss or earnings per share;

    - physical or non-financial measures such as number of employees, number of subscribers, sales per square meter (when sales figures are extracted directly from financial statements) or social and environmental measures such as greenhouse gases emissions, breakdown of workforce by type of contract or by geographic location;

    - information on major shareholdings, acquisition or disposal of own shares and total number of voting rights;

    - information to explain the compliance with the terms of an agreement or legislative requirement such as lending covenants or the basis of calculating the director or executive remuneration

Disclosure principles

20. **Issuers or persons responsible for the prospectus should define the APMs used and their components as well as the basis of calculation adopted, including details of any material hypotheses or assumptions used. Issuers or persons responsible for the prospectus should also indicate whether the APM or any of its components relate to the (expected) performance of the past or future reporting period.**

Presentation

21. **Issuers or persons responsible for the prospectus should disclose the definitions of all APMs used, in a clear and readable way.**

22. **APMs disclosed should be given meaningful labels reflecting their content and basis of calculation in order to avoid conveying misleading messages to users.**

23. For example, issuers or persons responsible for the prospectus should not use overly optimistic or positive labels such as ‘guaranteed profit’ or ‘protected returns’.

24. Issuers or persons responsible for the prospectus should not use labels, titles or descriptions of measures defined in the applicable financial reporting framework that are the same or confusingly similar when referring to APMs.

25. Issuers or persons responsible for the prospectus should not mislabel items as non-recurring, infrequent or unusual. For example items that affected past periods and will affect future periods will rarely be considered as non-recurring, infrequent or unusual (such as restructuring costs or impairment losses).

Reconciliations

26. **A reconciliation of the APM to the most directly reconcilable line item, subtotal or total presented in the financial statements of the corresponding period should be disclosed, separately identifying and explaining the material reconciling items.**

27. **Issuers or persons responsible for the prospectus should also present the most directly reconcilable line item, subtotal or total presented in the financial statements relevant for that specific APM.**

28. Where reconciling items are included in financial statements, users should be able to identify them in those financial statements. Where a reconciling item cannot be extracted directly from the financial statements, the reconciliation should show how the figure is calculated.

29. Where an APM is directly identifiable from the financial statements no reconciliation is required. This applies for example when an APM is a total or subtotal presented in financial statements.

30. Where financial statements of the corresponding period are not yet published, APMs should be reconciled to the most directly reconcilable line item, subtotal or total which will be included in those financial statements when they are published (e.g. earnings results presented before financial statements).

31. Where financial statements of the corresponding period are not going to be published, APMs should be reconciled to the most directly reconcilable line item, subtotal or total which would be included in those financial statements if they were published. The most directly reconcilable line item, subtotal or total used to reconcile the APM should be calculated and presented consistently with the corresponding line item, subtotal or total included in the issuer's most recent published annual financial statements.

32. Where an APM presented is not reconcilable because it does not derive from the financial statements, such as profit estimates, future projections or profit forecasts, the issuer should provide an explanation about the consistency of that APM with the accounting policies applied by the issuer in the financial statements prepared in accordance with the applicable financial reporting framework.

Explanation on the use of APMs

33. **Issuers or persons responsible for the prospectus should explain the use of APMs in order to allow users to understand their relevance and reliability.**

34. Issuers or persons responsible for the prospectus should explain why they believe that an APM provides useful information regarding the financial position, cash-flows or financial performance as well as the purposes for which the specific APM is used.

Prominence and presentation of APMs

35. APMs should not be displayed with more prominence, emphasis or authority than measures directly stemming from financial statements.

36. Presentation of APMs should not distract from the presentation of the measures directly stemming from financial statements.

Comparatives

37. **APMs should be accompanied by comparatives for the corresponding previous periods. In situations where APMs relate to forecasts or estimations, the comparatives should be in relation to the last historical information available.**

38. **Issuers or persons responsible for the prospectus should present reconciliations for all comparatives presented.**

39. Where it is impracticable to provide comparative figures, issuers or persons responsible for the prospectus should disclose its impracticability and explain why it is impracticable to provide those comparatives.

40. Where restating comparatives, issuers or persons responsible for the prospectus should only use information available at the end of the financial period for which the APM was presented, and should not incorporate effects of events occurring after that moment, i.e. hindsight should not be used when presenting restated comparatives.

Consistency

41. **The definition and calculation of an APM should be consistent over time. In exceptional circumstances where issuers or persons responsible for the prospectus decide to redefine an APM, the issuer should:**

    i. **Explain the changes;**

    ii. **explain the reasons why these changes result in reliable and more relevant information on the financial performance, and**

    iii. **provide restated comparative figures.**

42. **If an issuer stops disclosing an APM, the issuer should explain the reason for considering that this APM no longer provides relevant information.**

43. When a specific APM is replaced by another one that better achieves the same objectives, issuers should explain why the new APM provides reliable and more relevant information compared to the previous APM used.

44. APMs included in prospectuses should be used consistently for the financial periods covered by the prospectus. These guideline should not extend to where the persons responsible for the prospectus decides to replace an APM or to stop presenting an APM across different prospectuses in terms of time or the nature of securities being issued (e.g. persons responsible for the prospectus shall not be required to explain why different APMs are used in a prospectus for issuing equity securities and one for issuing non-equity securities taking into account the fact that the relevance of performance measurements may differ depending on the type of securities being issued).

Compliance by reference

45. **Except in the case of prospectuses which are covered by a separate regime for incorporation by reference[19] and except for those member states which do not permit the compliance by reference, disclosure principles set out in these guidelines may be replaced by a direct reference to other documents previously published which contain these disclosures on APMs and are readily and easily accessible to users. In this case, compliance with the guidelines is to be assessed reading the documents together. However, compliance by reference should not override the other principles of these guidelines**

46. APMs should be accompanied by the comparatives for the corresponding previous periods, thus the compliance by reference should not be understood as allowing the removal of those comparatives and replacement with references.

47. References made should direct users to the information required by these guidelines such as direct hyperlinks into the documents where the information may be accessed. This reference should be sufficiently precise such as identification of the specific page, section or chapter of the documents where this information can be read.

48. For the purpose of these guidelines, readily and easily access to the documents implies that investors will not need to register on websites, to pay fees to access this information or to search for these documents through a search facility or a succession of links.

[19] Article 11 of Directive 2003/71/EC.