

Reporting Earnings -- A New Model

After March 28, 2003, public companies reporting earnings must comply with new rules adopted by the SEC as part of its implementation of the Sarbanes-Oxley Act of 2002. These include new Item 12 of Form 8-K, which governs earnings announcements, and new Regulation G, which imposes conditions on the public disclosure of non-GAAP financial measures.¹ We recently issued an advisory describing these new rules. (See Covington & Burling advisory, dated February 24, 2003, [Conditions for Using Non-GAAP Financial Measures and Publicizing Earnings.](#))

In this advisory we review the current practices followed by many companies in publicizing their quarterly results. Next, we discuss how the SEC's new rules will affect those practices. Finally, we suggest a model for publicizing quarterly results that reflects the new requirements.² **Since we originally released this advisory, the SEC has provided additional guidance on the application of these rules and the use of non-GAAP financial measures.** See [Frequently Asked Questions Regarding the Use of Non-GAAP Financial Measures.](#)

Below is a brief summary of the more significant changes to the current model of publicizing earnings as a result of the new rules that are discussed in this advisory.

The Current Model	Changes in the Model After March 28
Press release to announce date and time of earnings call	Press release should also indicate location on company's website where financial information to be conveyed during earnings call with be posted.
Earnings press release	<p>Any "non-GAAP financial measures" included in the press release must be accompanied by</p> <ul style="list-style-type: none"> equally prominent presentation of most directly comparable GAAP measures; and reconciliation of differences between GAAP and non-GAAP measures. <p>In addition, the press release, the Form 8-K referred to below, or the company's most recent annual report (updated if necessary) must also include</p> <ul style="list-style-type: none"> statement of reasons why management believes non-GAAP measures provide useful information; and if material, statement of additional purposes for which management uses non-GAAP measures.

¹ See the SEC's adopting release of these rules, Release No. 33-8176 (Jan. 22, 2003). Regulation G consists of three new rules: Rule 100 (general rule), Rule 101 (definitions), and Rule 102 (no effect on fraud liability). See 17 C.F.R. § 244.100 *et seq.*

² This advisory is aimed at U.S. Public companies and does not address certain exceptions regarding the use of non-GAAP financial measures that are available to foreign private issuers. Further, we do not address various practices and issues that pertain to the impact of earnings releases on contemporaneous securities offerings.

The Current Model	Changes in the Model After March 28
Voluntary Form 8-K to file (or furnish) press release	Company <i>must</i> furnish press release on Form 8-K (Item 12) within five days. If company conducts earnings call, it can avoid additional Form 8-K filing for earnings call by furnishing the first Form 8-K to SEC before the earnings call takes place and holding the earnings call within 48 hours after company issues earnings release.
Earnings release posted on website	Press release or other document containing the required “comparable” and “reconciliation” disclosures for non-GAAP financial measures should be posted to company’s website, before call begins. This document should also include financial and statistical “earnings” information described in Item 12 of Form 8-K.
Earnings call	During call, company should inform audience of location on website where additional information regarding non-GAAP financial measures is posted. If, during call, company discloses different or additional financial information or non-GAAP financial measures that were not included in press release, it must post such information to website as soon as possible.
Call replay and/or web simulcast available	Website access to press release or other document containing required information described above, and/or call replay or web simulcast of call, should be maintained for at least 12 months.

The Current Model

Although practice varies depending on a variety of factors including company size, number and type of shareholders, industry, and stage of development, most public companies use a model containing some or all of the following elements in publicizing their quarterly and annual earnings.³

- Company Issues Initial Press Release to Announce Earnings Call.** After the end of the quarter, and at least several days before the scheduled quarterly earnings call, the company issues a press release to announce the date and time of the call. This release provides dial-in information for the call and may also include Web simulcast information and information about whether the call or simulcast will be replayed or continue to be made available. The company also usually posts this press release (or a similar announcement) prominently on its website.

³ This model has evolved over time and reflects “best practices” in light of applicable legal requirements, including (i) requirements imposed on listed companies by stock exchanges and Nasdaq to make prompt disclosure through the press of material information, including earnings information, and (ii) the SEC’s Regulation FD, which prohibits selective disclosure by public companies of material information such as earnings results.

- **Company Issues Earnings Press Release.** The evening before, or before the market opens on the morning of, the earnings call, the company issues a press release summarizing its results for the recently completed quarter. This press release typically contains a high level summary of key performance measures and a comparison with prior periods but does not address all items that would be included in the company's financial statements.⁴ Many companies include operating statistics and non-GAAP financial measures such as EBITDA (see #6 below). The release is not specifically required to be filed with the SEC, and, historically, companies generally have not done so.⁵ The earnings press release is normally posted on the investor relations page of the company's website on the day it is issued.
- **Company Holds Earnings Call.** The company conducts its earnings call, open to all who wish to listen. Typically, the company's senior officers first read from a prepared script, summarizing the quarterly results and elaborating on the information contained in the press release. Some companies hold a "listen only" call and do not field questions, while others field questions from investors and analysts following management's presentation.
- **Company Makes Call Replay and Web Simulcast Available.** After the call ends, the company typically makes a replay and/or Web simulcast available for some period of time.⁶

How Is the Model Changing After March 28, 2003?

The model for earnings announcements will change significantly after March 28, 2003. Some of these changes are mechanical, while others require deliberation and may require companies to modify or eliminate prior practices. In any event, companies with a December 31 fiscal year-end should carefully plan their upcoming earnings announcements for the quarter that will end on March 31, 2003. In doing so, companies should consider the following questions.

1. When Is a Form 8-K Required?

After March 28, 2003, a Form 8-K will *always* be required when a company makes a public announcement or release (whether written, oral or electronic) that discloses material non-public information regarding results of operations or financial condition for a *completed* quarterly or annual fiscal period.⁷ This is the case whether or not the release or announcement contains any non-GAAP financial measures (as defined

⁴ In many cases, the company's auditors will not have completed their review of the quarterly results by the time the press release is issued.

⁵ Some companies have filed press releases voluntarily, usually under Item 5 of Form 8-K, mainly to incorporate the release by reference into an active registration statement. Also, since 2000, companies seeking to satisfy the "public disclosure" requirement of Regulation FD have had the option of furnishing (or filing) the press release under Item 9 of Form 8-K, and companies with active registration statements have increasingly used Item 9, in lieu of Item 5, to incorporate interim earnings information into their active registration statements.

⁶ We understand that some companies also post transcripts of the call on their websites, although this practice is problematic.

⁷ Because Item 12 only applies to completed periods, public disclosure of earnings estimates that relate only to future or ongoing periods is not covered.

in Regulation G and discussed in #6 below). This imposes a new reporting obligation under the Securities Exchange Act of 1934 where before there was none.

The company must describe the earnings announcement or release briefly in the text of new Item 12 of Form 8-K and must attach the announcement or release as an exhibit to the Form 8-K. The company must *furnish* the Form 8-K to the SEC within five business days of the announcement or release. As a practical matter, however, companies that also hold a related earnings call are very likely to furnish the release on the same day the earnings release is issued (or within one day thereof), for the reasons discussed in #4 below.

2. What is the Significance of “Furnishing” the Release to the SEC Instead of “Filing” it?

Information “furnished” to—as opposed to “filed” with—the SEC under Item 12 enjoys certain advantages. First, it is not (unless the company states otherwise) subject to Section 18 of the Exchange Act, which imposes liability in certain circumstances for misleading statements made in SEC filings. Second, it is not (unless the company states otherwise) incorporated by reference into a registration statement, proxy statement, or other report filed with the SEC, thereby avoiding exposure of such information in some cases to the more stringent liability provisions in Sections 11 and 12(2) of the Securities Act of 1933. Finally, it is not subject to all of the requirements contained in recent amendments to Item 10 of Regulation S-K (specifically the prohibition on certain types of non-GAAP financial measures, which are discussed in #8 below).

As a technical matter, the amendments to Form 8-K are imprecise as to whether the SEC intends the entire report to be “furnished,” or merely the information included in the report (*i.e.* the earnings release or announcement). New General Instruction B(6) to Form 8-K states that the report “is required to be furnished,” and then goes on to state that “[t]he *information in a report* furnished pursuant to Item 12 shall not be deemed to be ‘filed’ for purposes of Section 18 of the Exchange Act” (emphasis added). Because a Form 8-K could relate to information that needs to be “filed” under items other than Item 12, together with information that is “furnished” under Item 12, it is probably analytically cleaner to think about the Item 12 information as being “furnished” under a report that is being “filed.”⁸

3. Can the Earnings Release be “Filed” Instead of Furnished?

Yes. Although the default position under Item 12 of Form 8-K is that the report is furnished to, not filed with, the SEC, in some circumstances a company may choose to “file” its earnings release. It could do so by indicating on the Form 8-K that it is being filed, not furnished, or by explicitly incorporating the report, or the information under Item 12, by reference into another of the company’s filings. It may, for instance, be advantageous to incorporate the Form 8-K into a registration statement under the Securities Act, to avoid having to file an amendment to such registration statement and/or prepare a prospectus supplement.

⁸ The substantive distinction between “furnished” and “filed” is not a new one. An annual report to security holders under Exchange Act Rule 14a-3 is to be mailed to the SEC “solely for its information” and is not deemed filed. Similarly, information furnished under Items 1, 2 and 3 of Part I of Form 10-Q and Item 9 of Form 8-K under the Exchange Act is not deemed filed, nor are the compensation committee report and the performance graph required by Item 402 of Regulation S-K and the audit committee report required by Item 306 of Regulation S-K.

4. Does the Form 8-K Requirement Apply to Oral, Telephonic and Similar Disclosures?

Yes, the new Form 8-K requirement applies to any communication, written, oral, telephonic, or by webcast, broadcast or similar means, if the communication includes material non-public information regarding results for a prior period. Thus, unless the company can fit within the exception described below, it must furnish to the SEC, on a separate Form 8-K, any material, non-public information disclosed during an earnings call.⁹

The SEC has provided a limited exception for disclosures that are made as part of oral, telephonic or similar presentations following prior announcements of results that were the subject of a Form 8-K filing. Under this exception, a separate Form 8-K need *not* be furnished, if:

- the oral, telephonic or similar disclosures are (i) part of a presentation that is complementary to a related written earnings announcement or release¹⁰, (ii) such disclosure occurs within 48 hours after the issuance of the written release or announcement, and (iii) the written release or announcement was furnished to the SEC on Form 8-K *before* the presentation;
- the oral, telephonic or similar presentation is announced by a broadly distributed press release that indicated when and precisely where on the company's website the information would be posted;
- the presentation is widely available to the public by means of an open conference call, webcast, etc.; and
- the financial and other statistical information contained in the oral, telephonic or similar presentation is posted on the company's website, along with any additional information necessary under Regulation G if the presentation includes non-GAAP financial information.¹¹

As a practical matter, therefore, companies that want to avoid filing a separate Form 8-K will schedule the earnings call to occur within no less than 48 hours of the issuance of the written earnings release. Further, these companies will furnish their earnings release on Form 8-K to the SEC promptly after its issuance to ensure receipt by the SEC before the earnings call begins.

⁹ The mere repetition of information that was publicly disclosed previously, or the release of the same information in a different form, does not trigger the Item 12 requirement. Also, by its terms the new Item 12 requirement only applies to information that is *material*.

¹⁰ In its adopting release, the SEC interprets the word *complementary* narrowly and cautions that this exception is not intended to allow disclosure of *material* earnings information to be shifted from the written release or announcement to the oral or telephonic presentation. Information that goes beyond the financial information disclosed in the earnings release, but is complementary thereto, may be provided during the earnings call, as long as such information is posted to the company's website.

¹¹ According to the SEC's adopting release, such information should remain posted on the website on an ongoing basis, for a minimum of 12 months.

5. What if Non-GAAP Financial Measures are Included in Earnings Announcements?

Written Disclosure. If “non-GAAP financial measures” (as defined in Regulation G and discussed in #6 below) are included in a publicly disclosed *written* document containing material information, such as an earnings release, the non-GAAP financial measures must be accompanied by¹² the following complementary presentation:

- an equally prominent presentation of the “most directly comparable” financial measures according to GAAP; and
- a reconciliation of the differences between the GAAP and non-GAAP measures.¹³

In addition, the company must provide the following disclosures in the earnings release, the Form 8-K with which the earnings release is furnished to the SEC, or the most recent annual report filed with the SEC (provided that the company updates such disclosures, as necessary, no later than the time the Form 8-K report is filed):

- a statement disclosing the reasons why management believes that the non-GAAP financial measures provide useful information to investors¹⁴; and
- to the extent material, a statement disclosing the additional purposes, if any, for which management uses the non-GAAP financial measures that are not covered by the statement above.

Non-Written Disclosure. If non-GAAP financial measures are released orally or by telephone, webcast, broadcast or similar media, such as during a quarterly earnings call, the company must provide the same disclosures described above regarding the “most directly comparable” financial measures according to GAAP and a reconciliation of the differences between the GAAP and non-GAAP measures. This obligation may be satisfied by posting the required comparative and reconciling presentation on the company’s website and, during the presentation, informing the audience of the availability and location of that additional information. The company must post the information by the time the non-GAAP financial measure is made public. This presentation should remain posted on the company’s website on an ongoing basis, and the SEC has indicated that website access should continue for a minimum of 12 months.

These requirements do not apply to the disclosure of non-GAAP financial measures if the disclosure is part of a communication that is subject to the SEC’s rules for communications regarding business combination transactions.

¹² The SEC’s use of the word “accompany” suggests that the required disclosures should appear in the same location as the non-GAAP financial measures.

¹³ In general, this reconciliation must be quantitative, for both the historical information and any forward-looking information presented. However, quantitative reconciliation of forward-looking information is required only “to the extent available without unreasonable efforts.” Separately, the registrant must identify what information is not available and disclose its probable significance.

¹⁴ In its adopting release, the SEC has said that the fact that the non-GAAP financial measure is useful to analysts cannot be the sole support for management’s statement as to why investors may find the non-GAAP measure useful. Of course, realistically public companies must be cognizant of, and responsive to, requests made by their investors. Given the SEC’s disdain for “boilerplate” justifications, however, companies using non-GAAP financial measures are well advised to provide specific, defensible reasons for using such measures, based on demonstrable benefits realized by management, analysts or others.

6. What Is a Non-GAAP Financial Measure?

Non-GAAP financial measures are financial measures which, while not prepared in accordance with GAAP, are often derived from GAAP measures and are intended to show useful information about a company's financial performance, position or cash flows. Companies and analysts have commonly referred to these non-GAAP measures as "pro forma" information, but the SEC has asserted its preference for the term "non-GAAP financial measures" to avoid confusion with the use of the term "pro forma" in other contexts, such as Article 11 of Regulation S-X.

Regulation G defines a non-GAAP financial measure as "a numerical measure of a registrant's historical or future financial performance, financial position or cash flow" that either excludes amounts that "the most directly comparable GAAP measure" would have included or, alternatively, includes amounts that the comparable GAAP measure would have excluded. The definition captures all measures that depict a company's performance over time or liquidity differently than the comparable GAAP-based presentations.

The definition expressly excludes operating and other statistical measures, as well as ratios or statistical measures, calculated using exclusively one or both of (i) financial measures, calculated in accordance with GAAP and (ii) operating or other measures that are not non-GAAP financial measures. The definition also excludes financial measures that must be disclosed to satisfy GAAP, SEC rules or other regulatory requirements.¹⁵

A prime example of a non-GAAP financial measure is EBITDA (earnings before interest, taxes, depreciation and amortization). While EBITDA could be calculated using elements derived from GAAP financial statements, it is not a measure presented in accordance with GAAP. Many companies (and the investors and analysts who follow them) believe that EBITDA, by excluding "non-operating" charges, provides a truer indication of the company's underlying performance from operations and outlook for profitability, than do GAAP measures such as net income and income from operations.¹⁶ Another example of a non-GAAP financial measure would be a measure of operating income that excludes one or more non-recurring expense or revenue items.

Many companies use other non-GAAP financial measures in their earnings releases, periodic SEC reports and other SEC filings. For example, real estate investment trusts (REITs) commonly report FFO (funds from operations), and many companies with significant capital expenditures report "free cash flow."

¹⁵ The SEC's adopting release gives the following examples of measures that would fall outside the definition: statistics such as unit sales and numbers of employees, subscribers, or advertisers; expected indebtedness amounts; amounts of planned-but-unmade repayments; estimated revenues or costs of a new product line (if those amounts were estimated in the same way as under GAAP); measures of profit, loss, or total assets for each segment that must be disclosed under GAAP; and regulatory capital measures for financial institutions.

¹⁶ For example, in a recent earnings release, Nextel Communications explained that it reports EBITDA because it believes that EBITDA "is a primary measure of operating performance and that growth in EBITDA is an indicator of future profitability, especially in a capital intensive industry such as wireless telecommunications."

7. How Should Non-GAAP Financial Measures be Reconciled to GAAP Measures?

Companies using non-GAAP financial measures must disclose the most directly comparable GAAP equivalents and provide a reconciliation between the two sets of measures. In some cases, this will be straightforward, as, for example, in the case of an income statement item that excludes a non-recurring expense. In other cases, the most directly comparable GAAP equivalent measure is not as clear. For example, EBITDA ostensibly is a measure of “earnings,” *i.e.* performance over time and, thus, comparable to income statement items. Many companies and the analysts who follow them, however, also use EBITDA to help assess the company’s available cash (*i.e.* cash from operations). For its part, the SEC has indicated that (i) non-GAAP financial measures that reflect cash or “funds” generated from operations (liquidity) should be balanced with disclosure of amounts from the statement of cash flows (cash from operating, investing and financing activities), and (ii) non-GAAP financial measures that depict performance should be balanced with net income, or income from continuing operations, taken from the income statement or statement of operations.¹⁷

8. Can Non-GAAP Financial Measures be Used in SEC Filings?

When it adopted Regulation G, the SEC also adopted amendments to Item 10 of Regulation S-K, governing the use of non-GAAP financial measures in SEC filings. These amendments prohibit certain non-GAAP financial measures and practices in SEC filings. The non-GAAP financial measures and practices that are prohibited by amended Item 10 in SEC filings are not included in Regulation G and, therefore, are not explicitly prohibited in non-filed communications such as earnings releases furnished on Form 8-K.

Amended Item 10 of Regulation S-K prohibits the use of the following in SEC filings:

- non-GAAP liquidity measures that exclude charges or liabilities requiring cash settlement (or that would have required such settlement without an alternative means of settlement), except for EBIT and EBITDA measures (which can be used);
- non-GAAP measures calculated by removing or smoothing items described as infrequent or non-recurring if either (1) the type of charge or gain is reasonably likely to recur within two years or (2) a similar charge or gain occurred within the previous two years;
- presentation of non-GAAP financial measures on the face of the company’s GAAP financial statements or corresponding notes;
- presentation of non-GAAP financial measures on the face of any pro forma financial information disclosed to satisfy Article 11 of Regulation S-X; and

¹⁷ The issue of whether EBITDA is a performance measure or liquidity measure is also addressed, indirectly, by amended Item 10 of Regulation S-K, which states that registrants must not exclude charges requiring cash settlement from non-GAAP *liquidity* measures, other than EBIT or EBITDA. The implication is that EBIT and EBITDA are liquidity, or cash flow, measures and not performance measures.

- use of titles or descriptions of non-GAAP financial measures that are identical or confusingly similar to those used for GAAP financial measures.¹⁸

One of the likely effects of the foregoing amendments to Item 10 will be to reduce certain uses of “adjusted EBITDA” measures, *i.e.* EBITDA that is adjusted to back out non-recurring items such as restructuring charges, gains and losses from asset sales outside the ordinary course of business, write-offs, and similar items. While amended Item 10 does permit companies to report EBIT and EBITDA measures in filed SEC documents, it prohibits adjustments for events described as “infrequent or non-recurring” where the type of charge or gain is reasonably likely to recur within two years or a similar charge or gain occurred within the prior two years.¹⁹

9. Will Amended Item 10 of Regulation S-K Affect Earnings Release Practices?

Concerns About Section 10(b). The non-GAAP financial measures prohibited by Item 10 are not prohibited in non-filed earnings announcements. The SEC has indicated that these prohibitions were purposefully left out of Regulation G to address concerns voiced by commenters that companies would be reluctant to continue using non-GAAP financial measures in their earnings announcements if the prohibitions were included in Regulation G. Nonetheless, in light of the prohibitions on specific types of non-GAAP financial measures and practices in amended Item 10, companies should be careful to use non-GAAP financial measures in their non-filed earnings announcements only in a manner that does not run afoul of Regulation G’s anti-fraud provision and the general anti-fraud provisions of Section 10(b) of the Exchange Act.²⁰ For example, the SEC staff has informally indicated that it is skeptical of any financial measurement that eliminates a recurring part of a company’s operations and that it intends to look very closely at such a measure, particularly the discussion of how management expects investors to use it and how management uses it.²¹

If a company presents a non-GAAP measure that is adjusted for non-recurring items and such adjustment would not be permitted by amended Item 10 in an SEC filing, the company should, at a minimum, balance such presentation with a reconciliation of such measure to the most directly comparable GAAP measure, clearly showing how the “non-recurring” items are added back. A company using this type of measure also should

¹⁸ In response to significant comment, the SEC dropped from this list of prohibitions the use of non-GAAP per share measurements. Nevertheless, per share measures that are prohibited specifically under GAAP or other SEC rules remain prohibited in SEC filings.

¹⁹ The SEC exempted EBIT and EBITDA from the prohibition set forth in amended Item 10 of Regulation S-K because of “their wide and recognized existing use.” The SEC has offered no discussion, however, of whether, and to what extent, variations in the precise definitions of such terms might be permissible, including variations that take account of certain adjustments. The SEC’s reference to the “wide and recognized existing use” of such terms might be read to imply the acceptance of a variety of definitions for the terms, based on existing practice.

²⁰ Prior to the Sarbanes-Oxley Act, the SEC was already quite concerned with potentially misleading use of “pro forma” (*i.e.* non-GAAP) financial information. For example, in cautionary advice issued in late 2001, it stated, among other things, that a company purporting to show earnings before “unusual or nonrecurring transactions” should describe the particular transactions and apply the methodology described when presenting purportedly comparable information about other periods. See [Release No. 33-8039](#) (Dec. 4, 2001).

²¹ Not all recurring exclusions are unacceptable. For example, the SEC staff has indicated that the S&P core earnings measure, which is intended to depict core earnings by removing investment gain or loss related to the company’s pension plan, is acceptable. Conversely, a non-GAAP measure that eliminates merger related charges where the company has a stated growth plan through acquisitions is not acceptable, according to the staff.

be careful to identify and present *all* material non-recurring items for such measure (both expense and revenue),²² and it should provide credible, non-boilerplate reasons why management believes the non-GAAP measure provides useful information to investors. Some companies considering whether to use such measures in their earnings announcements may, with good reason, choose to take a “wait and see” approach for the time being and refrain from using such measures until further guidance becomes available.

Incorporation of Earnings Announcements into Other SEC Filings. A second consequence of amended Item 10 arises where a company wishes to incorporate its earnings announcement into another of its SEC filings. If the earnings announcement contains non-GAAP financial measures or practices that are prohibited by amended Item 10, then such announcement cannot be incorporated by reference into another SEC filing (or, if so incorporated, such other filing presumably would not comply with the applicable form requirements). Companies wishing to incorporate earnings announcements into their other SEC filings should take care to comply with the requirements of amended Item 10 in presenting any non-GAAP financial measures in earnings releases.

Tension with Heightened MD&A Disclosure Requirements. For some companies, the new rules will either prohibit the use of, or persuade companies not to disclose, certain non-GAAP financial measures in their SEC filings or earnings announcements, even though such non-GAAP financial measures may relate directly to other arrangements that are material to an understanding of financial results or condition. For example, many companies with outstanding high yield debt must satisfy financial covenants which usually include quarterly adjusted EBITDA targets or targets based on other non-GAAP financial measures. This may also be true with respect to other credit arrangements, including credit rating triggers. Disclosure of many of these types of non-GAAP financial measures will be constrained by amended Item 10 and/or Regulation G. However, in a January 2002 statement calling for improved MD&A disclosure, the SEC urged public companies to consider disclosing, among other items, provisions in debt instruments that could trigger requirements for early payment, additional collateral support, changes in terms, acceleration of maturity, default or creation of additional financial obligations.

Public companies will need to balance the new restrictions on disclosing non-GAAP financial measures with the countervailing requirement to make meaningful, forward-looking disclosures about their liquidity and capital resources, which may necessitate discussion of applicable debt covenants and the company’s performance with respect to such covenants in prior and future periods. In general, the obligation to disclose factors that are material to the company and its liquidity and financial resources should outweigh the new restrictions on use of non-GAAP financial measures, provided that any such use of non-GAAP measures is relevant to the topic being discussed in the MD&A and that the disclosure makes clear that such use of non-GAAP measures is limited to the specific context of such discussion.

²² In its enforcement action against Trump Hotels & Casino Resorts Inc., the SEC alleged that the company’s use of “pro forma” results in its quarterly earnings release was misleading because although it specifically excluded a one-time charge, it failed to disclose that it also included a material one-time gain associated with the termination of a lease. See *In the Matter of Trump Hotels & Casino Resorts Inc.*, [Release No. 34-45287](#) (Jan. 16, 2002).

Selective Disclosure Concerns. Separately, companies will need to wrestle with the issue of selective disclosure. A company that does not include non-GAAP financial measures in its public earnings announcements or SEC filings may nevertheless be required to disclose such information to the holders of its high yield debt (or the agent for such holders) or other lenders, to permit such parties to assess the company's compliance with such covenants. Companies in this situation should be mindful of selective disclosure concerns and should take care to comply with Regulation FD.

10. Should Companies Consider Changing Their Internal Processes for Preparing and Reviewing Earnings Releases?

All public statements, including earnings releases, must be considered subject to the general anti-fraud provisions of the federal securities laws. The new requirement to deliver the earnings release to the SEC, on a report signed by an officer of the company, presents a good opportunity for companies to incorporate, to the extent they have not already done so, the preparation of quarterly earnings announcements into their regular disclosure and internal controls. In addition, companies that have not previously involved their audit committees in reviewing quarterly earnings announcements may wish to do so.

Further, as audit practices and standards continue to evolve, the new Form 8-K requirement may lead to increased, and/or earlier, involvement by outside auditors in the preparation and review of their clients' quarterly earnings announcements. Impetus for such change may come from pressure exerted by one or more interested stakeholders, such as directors, institutional shareholders, analysts, lenders, underwriters, or even auditors themselves. For example, companies that have not done so previously might ask their auditors to review their draft earnings announcements before they are released. It is also conceivable that some companies might choose to delay their earnings announcements until their auditors complete a full review of the company's quarterly results. This would represent a significant change from current practice and would delay the release of earnings announcements by companies following this practice by several days, if not weeks.²³

A New Model - Earnings Announcements With Non-GAAP Financial Measures

We expect that many, if not most, public companies that have traditionally used EBITDA or other non-GAAP financial measures in their regular earnings announcements will wish to continue to do so, not only because such companies view these measures to be useful indicators of performance or condition, but also because investors and analysts who follow such companies have come to expect and rely on such measures.

As for the mechanics of making earnings announcements with non-GAAP financial measures after March 28, 2003, the following model may offer guidance to companies seeking to navigate, and comply with, the new requirements.

- **Company Issues Initial Press Release to Announce Earnings Call.** In addition to the dial-in number and other logistical information traditionally provided in this release, the announcement should indicate the specific location (using site location or link title) on the company's website where the company will post the financial and other statistical information to be conveyed during the

²³ Also, one of the byproducts of the shortened Form 10-Q filing deadlines being phased in may be added pressure to collapse the current time lag between earnings announcements and the filing of the Form 10-Q.

earnings call.²⁴ Companies will need to take the necessary steps to ensure that, prior to the issuance of the initial press release, their websites are configured in a way that is consistent with the instructions to be included in the press release, *i.e.* when the time comes to post the required material to the website, the material will be able to be posted to the precise location indicated in the press release.

- Company Issues Earnings Press Release.** The evening before, or before the market opens on the morning of, the earnings call, the company should issue a press release summarizing its results for the recently completed quarter. Any non-GAAP financial measures included in the press release must be accompanied by (i) a presentation, just as prominent as the non-GAAP financial measures, of the “most directly comparable” GAAP financial measures, and (ii) a reconciliation of the differences between the GAAP and non-GAAP measures. In addition, the company must include, in the press release, the Form 8-K, or its most recent annual report filed with the SEC (provided that the company updates such disclosures, as necessary, no later than the time the Form 8-K is filed), (a) a statement disclosing the reasons why management believes that the non-GAAP financial measures provide useful information to investors, and (b) to the extent material, a statement disclosing the additional purposes, if any, for which management uses the non-GAAP financial measures that are not covered by the statement above.
- Company Furnishes Earnings Release to SEC on Form 8-K.** The company should furnish the press release containing the earnings announcement to the SEC under Item 12 of Form 8-K *before* the earnings call takes place and should schedule the earnings call to take place within 48 hours after issuing the earnings release.²⁵ This means that most companies will likely schedule the earnings call to occur within 24 hours (or less) after the press release is issued and, further, that most companies will likely furnish the Form 8-K to the SEC promptly after the earnings release is issued, to ensure receipt by the SEC before the earnings call begins. Companies will need to take the necessary steps to ensure that the Form 8-K is completed as soon as possible after the issuance of the press release, so that it can be converted to the appropriate format for transmission through EDGAR, the SEC’s electronic filing system.
- Company Posts Press Release to Website.** Before the call begins, the company should ensure that all of the information that it plans to disclose during the earnings call and which is required to be posted to the company’s website, *i.e.* the “comparable” and “reconciliation” disclosures with respect to any non-GAAP financial measures and the other financial and statistical information contemplated by Item 12 of Form 8-K, is included in a single document. For practical purposes, this will usually be the earnings press release. The company should post this document to its website, before the call begins, at the location specified in the initial press release announcing the earnings call.

²⁴ The SEC urges companies to use the investor relations page of its website for these postings.

²⁵ This will allow the company to avoid having to file two Form 8-K reports - one for the written release and one for the earnings call. The Form 8-K that is furnished to provide the information required under Item 12 could also satisfy a company’s obligation under Regulation FD, as long as the Form 8-K were filed within the time frame required by Regulation FD and the Form 8-K indicated that it was also being furnished (or filed) under Item 9.

- **Company Holds Earnings Call.** The company conducts its earnings call. The call should be open to all who wish to listen. During the earnings call, the company must inform the audience of the availability and location on its website of the additional information regarding non-GAAP financial measures (i.e. the “comparable” and “reconciliation” disclosures).
- **Company Posts Additional Information Disclosed During Earnings Call to Website.** If, during the earnings call, the company discloses different or additional financial or other statistical information or additional non-GAAP financial measures that were not included in the written press release, the company must post that additional information, as well as the accompanying information required under Regulation G, to its website as soon as possible during or after the earnings call.²⁶ To satisfy this requirement, the company may make a replay of the call available on its website (as long as all of the required information, including the Regulation G information, is provided during the call), or it may create a separate document containing the required information and post that document to its website. Special care should be taken to avoid or minimize disclosure of any different or additional non-GAAP financial measures during the call, since the accompanying “comparable” and “reconciliation” information is required by Regulation G to be posted to the company’s website “at the time the non-GAAP financial measure is made public.”²⁷
- **Company Makes Replay and Web Simulcast Available.** After the call ends, the company can make a replay of the call, and the web simulcast of the call, available for some period of time. If any additional or different non-GAAP financial measure or other financial information was disclosed during the earnings call that was not included in the earnings release, the company should ensure that such information, as well as any accompanying information required by Regulation G, is posted to its website as soon as practical, during or following the call.
- **Company Maintains Press Release and/or Call Replay on Website for at Least 12 Months.** The information posted to the company’s website as described above should remain there on an ongoing basis, and the SEC has indicated that website access should continue for a minimum of 12 months.

²⁶ The company may also need to consider whether the release of additional material non-public information independently requires the company to take further action to disseminate the information to the public in order to comply with Regulation FD.

²⁷ Companies that provide a simulcast of the earnings call on their own websites should satisfy this simultaneous posting requirement, as long as all of the required information, including the “comparable” and “reconciliation” information required by Regulation G for any non-GAAP financial measures, is provided during the call. In cases where a company inadvertently discloses non-GAAP financial measures during an earnings call and is not able to post the information required by Regulation G at the time of such disclosure, the SEC staff has indicated informally that it will be acceptable to post such required information as soon as practical following the earnings call, normally by the end of the same day.

Conclusion

The new requirements with respect to earnings releases represent a major change in the landscape. Practices are certain to change in significant ways. In many respects, larger public companies will likely find it easier to deal with the new requirements, since such companies generally have greater investor relations, technical and other resources than do smaller companies. While the new Form 8-K requirement will increase public access to earnings releases and similar announcements, it remains to be seen how the new restrictions on use of non-GAAP financial measures will affect the quality and quantity of information available to investors.

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