Canadian Securities Administrators Autorités canadiennes en valeurs mobilières

CSA Second Notice and Request for Comment

Proposed National Instrument 52-112 Non-GAAP and Other Financial Measures Disclosure

Proposed Companion Policy 52-112 Non-GAAP and Other Financial Measures Disclosure

Related Proposed Consequential Amendments and Changes

February 13, 2020

Introduction

The Canadian Securities Administrators (the **CSA** or **we**) are publishing for a 90-day comment period the following materials:

- Revised version of proposed National Instrument 52-112 *Non-GAAP and Other Financial Measures Disclosure* (the **Proposed Instrument**);
- Revised version of proposed Companion Policy 52-112 *Non-GAAP and Other Financial Measures Disclosure* (the **Proposed Companion Policy**);
- Related proposed consequential amendments or changes to:
    - Multilateral Instrument 45-108 *Crowdfunding*[1];
    - Companion Policy 45-108CP *Crowdfunding*;
    - Companion Policy 51-102CP *Continuous Disclosure Obligations*;
    - Companion Policy 51-105CP *Issuers Quoted in the U.S. Over-the-Counter Markets*[2];
    - Companion Policy 52-107CP *Acceptable Accounting Principles and Auditing Standards*.

(collectively, the **Proposed Materials**).

The Proposed Instrument sets out disclosure requirements for non-GAAP financial measures, non-GAAP ratios, and other financial measures (i.e., capital management measures, supplementary financial measures, and total of segments measures, as defined in the Proposed Instrument).

[1] The securities regulatory authorities in British Columbia, Prince Edward Island, Newfoundland and Labrador, Northwest Territories, Yukon Territory and Nunavut are not proposing these consequential amendments or the changes to the related Companion Policy because MI 45-108 does not apply in these jurisdictions.

[2] The Ontario Securities Commission is not proposing this consequential change as Multilateral Instrument 51-105 *Issuers Quoted in the U.S. Over-the-Counter Markets* and its Companion Policy do not apply in Ontario.

The original versions of the Proposed Materials (the **Original Materials**) were first published on September 6, 2018. During the 90-day comment period we conducted 38 outreach sessions across seven cities in Canada allowing us to actively engage with stakeholders. The comment period ended on December 5, 2018. We received 42 comment letters from various stakeholders, including issuers, investors, accounting firms, standard setters, industry associations and law firms. The list of commenters is attached as Annex A. We wish to thank all commenters for contributing to the consultation. A summary of the comments we received and our responses to those comments are attached as Annex B. In response to the feedback we received, we have reduced the scope of the application of the Proposed Instrument and simplified the disclosure requirements, with the aim of ensuring investors receive appropriate disclosure without an overall increase in regulatory burden.

We understand that non-GAAP financial measures, non-GAAP ratios, and other financial measures can provide valuable information to investors when supplemented with useful disclosures. Considering the substantive changes made in response to comments received on the Original Materials, we are publishing the Proposed Instrument and the Proposed Companion Policy for a second comment period. We are also publishing for information the related proposed consequential amendments or changes in their original form.

The text of the Proposed Materials is contained in Annexes D through J of this Notice. Local amendments, if any, are in Annex K of this Notice. This Notice will also be available on the websites of CSA jurisdictions, including:

www.lautorite.qc.ca
www.albertasecurities.com
www.bcsc.bc.ca
nssc.novascotia.ca
www.fcnb.ca
www.osc.gov.on.ca
www.fcaa.gov.sk.ca
www.mbsecurities.ca

Summary of Changes to the Original Materials

Many comment letters expressed support for the objectives of the Original Materials. Commenters agreed with the analysis that non-GAAP financial measures and other financial measures disclosures lack standardized meaning under financial reporting frameworks, lack context when disclosed outside of the issuer's financial statements, and lack transparency as to their calculation or vary significantly by issuer and industry. However, concerns were expressed on the application and scope of the Proposed Instrument, definitions proposed, and perception of increased regulatory burden that the Proposed Instrument would have in comparison to current CSA Staff Notice 52-306 (Revised) *Non-GAAP Financial Measures* (**SN 52-306**), and SEC rules.

Following our extensive review and analysis of the comment letters, through the substantive changes to the Original Materials, we have aimed to:

- reduce the scope of application to certain issuers,
- exempt certain disclosures, financial measures, and types of documents,
- narrow and clarify various definitions,

- simplify the disclosure for non-GAAP financial measures that are forward-looking information and non-GAAP ratios,
- limit disclosures for capital management measures and total of segments measures,
- permit cross-referencing in certain circumstances,
- better align disclosure requirements with those adopted by other securities regulators,
- enhance readability, and
- reduce uncertainty regarding disclosure obligations by clarifying disclosure requirements and including significant guidance.

More information on the changes made in the Proposed Instrument is included in Annex C.

A second publication for comment will allow for stakeholder input on these changes.

Substance and Purpose

The Proposed Instrument addresses the disclosure surrounding non-GAAP financial measures, non-GAAP ratios, and other financial measures.

In some cases, non-GAAP financial measures, non-GAAP ratios, and other financial measures are helpful to investors to assess an issuer's financial performance. The Proposed Instrument does not contain specific limitations or industry-specific requirements; rather, it provides clarity and consistency with respect to an issuer's disclosure obligations and improve the quality of information provided to investors.

We acknowledge that some stakeholders continue to prefer that we

- limit, in specific circumstances, the disclosure of certain financial measures, and
- develop industry-specific requirements for certain financial measures.

However, due to the numerous types of ever-evolving financial measures disclosed across a range of industries, we continue to believe that disclosure requirements are best suited to respond to investor needs for quality information without being overly prescriptive. These requirements would allow investors to better analyze different financial measures within an industry or among different industries.

Although the definition of a non-GAAP financial measure has been clarified, the Proposed Materials have substantially incorporated the disclosure guidance in SN 52-306 for non-GAAP financial measures.

To ensure investors appreciate the context of capital management measures and total of segments measures, the Proposed Instrument introduces disclosure requirements if such financial measures are disclosed outside of the financial statements.

Background

Non-GAAP Financial Measures

Various activities have contributed to the development of the Proposed Materials, which are intended to replace the guidance provided in SN 52-306.

Many issuers, in all industries, disclose a range of financial measures that may lack standardized meanings under the financial reporting framework used in the preparation of the issuer's financial statements and lack transparency as to their calculation or vary significantly by issuer and industry.

Common terms used to label non-GAAP financial measures may include "adjusted earnings", "adjusted EBITDA", "free cash flow", "pro forma earnings", "cash earnings", "distributable cash", "cost per ounce", "adjusted funds from operations" and "earnings before non-recurring items".

In Canada, the guidance in SN 52-306 is intended to help ensure that non-GAAP financial measures (including ratios that include non-GAAP financial measures) do not mislead investors. Although we have updated SN 52-306 several times to respond to changing circumstances and published various staff notices and reports that comment on the topic, we continue to find that disclosure practices surrounding non-GAAP financial measures vary. Our findings are consistent with those of other stakeholders (particularly investors) who share our desire for quality disclosure.

The use of non-GAAP financial measures is a topic raised frequently by the financial reporting community, locally and abroad. In Canada, several organizations have undertaken research and issued guidance on how to disclose non-GAAP financial measures. Stakeholders generally have expressed the view that regulating the use of non-GAAP financial measures as primarily a task of the CSA.

We are aware the International Accounting Standards Board (IASB) has recently issued an exposure draft, as part of its Primary Financial Statements project, on General Presentation and Disclosures. This exposure draft could, among other things, change the structure and content of the income statement and result in some traditional non-GAAP financial measures being included in a note to the financial statements with accompanying disclosure. As the IASB proposals are at an early stage, it is difficult to determine what changes, if any, will be made to International Financial Reporting Standards (IFRS) requirements. We will monitor the progress of the exposure draft and the overall project in order to consider whether any changes to securities legislation will be appropriate.

Internationally, securities regulators are strengthening their efforts to regulate non-GAAP financial measure disclosure, including the International Organization of Securities Commissions (IOSCO) and the European Securities Markets Authority (ESMA). In addition, the U.S. Securities and Exchange Commission (SEC), which has formalized requirements for disclosure of non-GAAP financial measures in its rules, continues to provide further guidance on how to comply with applicable requirements.

Other Financial Measures

Over the years, we have also found that other financial measures that do not meet the definition of a non-GAAP financial measure in the Proposed Instrument present similar issues if not accompanied by appropriate disclosure. Such financial measures include certain measures disclosed in the notes to the financial statements that lack context when disclosed outside of the financial statements.

For example, IFRS permits disclosure of a broad range of capital management or segment measures but do not specify how such measures must be calculated in most circumstances. As a result, such measures can differ materially from amounts presented in the primary financial statements and may not be prepared in accordance with the recognition and measurement accounting policies used to prepare the issuer's primary financial statements.

To ensure investors were not confused or mislead, such measures were frequently identified as "non-GAAP" and issuers provided disclosures consistent with our expectations in SN 52-306. To ensure investors continue to appreciate the context of such measures, the Proposed Instrument includes disclosure requirements for such measures when disclosed outside of the financial statements. Consistent with the Original Materials, these disclosures are tailored for each measure and would require substantially less disclosure than expected under SN 52-306.

Anticipated Costs and Benefits of the Proposed Instrument

Overview

Cost benefit considerations have been informed by comments received in response to the Original Materials, as well as feedback received during related stakeholder outreach sessions. In addition, the Proposed Instrument has been developed in the context of various initiatives to reduce regulatory burden which, among other things, aim to ensure that regulatory costs are proportionate to the regulatory objectives sought.

We believe the Proposed Instrument results in a cost-effective and proportionate regulatory framework that supports innovation and competition while maintaining appropriate investor protections.

Although the Proposed Instrument codifies disclosures for non-GAAP financial measures and introduces targeted disclosure requirements for other financial measures, on balance, we believe, the Proposed Instrument and the Proposed Companion Policy result in an overall net reduction in regulatory burden, particularly in the long-term, because compared to current regulatory expectations as outlined in SN 52-306, the Proposed Instrument and the Proposed Companion Policy aim to:

- limit the application to certain issuers,
- exempt certain disclosures, financial measures, and documents,
- remove categorization of certain measures as non-GAAP financial measures,
- reduce and simplify disclosures for certain non-GAAP financial measures,
- eliminate duplication, in certain areas, through targeted provisions of incorporating information by reference,

- reduce uncertainty regarding disclosure obligations, and
- diminish the time and effort investors spend on understanding certain financial information.

We considered costs and benefits in limiting the application of the Proposed Instrument to certain issuers and in the process of identifying and disclosing non-GAAP and other financial measures.

Affected Stakeholders

Issuers

The Proposed Instrument only applies if an issuer that is within the scope of the Proposed Instrument discloses non-GAAP or other financial measures. If such an issuer does not disclose such measures, there is no effect.

Currently, disclosure expectations in SN 52-306 apply to all issuers that disclose non-GAAP financial measures. In contrast, the Proposed Instrument limits the application to certain issuers, such as reporting issuers. Investment funds, SEC foreign issuers, and designated foreign issuers are exempted – a significant reduction in scope.

Investors

We expect investors (institutional and retail) to be the primary beneficiaries of the Proposed Instrument because the Proposed Instrument:

- addresses many of the identified investor concerns,
- enhances the consistency, comparability and transparency of disclosure,
- reduces information-asymmetry, and
- diminishes the time and effort historically required to understand certain financial information (i.e., investor regulatory burden will be reduced).

Investors are not expected to incur additional costs.

Local Matters – Ontario

Authority for the Proposed Instrument

In Ontario, the rule-making authority for the Proposed Instrument is in paragraphs 13, 16, 22, 22.1, 25 and 39 of subsection 143(1) of the *Securities Act* (Ontario).

Alternatives Considered

We considered adopting the Original Materials in their original form as well as the alternatives suggested by the commenters as detailed in Annex B.

Reliance on Unpublished Studies

In developing the Proposed Instrument, we are not relying on any significant unpublished study, report or other written material.

Request for Comments

We welcome your comments on the Proposed Materials.

Please submit your comments in writing on or before May 13, 2020. If you are not sending your comments by email, please send us an electronic file containing submissions provided (in Microsoft Word format).

Address your submission to all of the CSA as follows:

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission (New Brunswick)
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Superintendent of Securities, Nunavut

Deliver your comments only to the addresses below. Your comments will be distributed to the other participating CSA.

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19th Floor, Box 55
Toronto ON M5H 3S8
Fax: 416-593-2318
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Corporate Secretary and Executive Director, Legal Affairs
Autorité des marchés financiers
Place de la Cité, tour Cominar
2640, boulevard Laurier, bureau 400
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Please refer your questions to any of the following:

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We cannot keep submissions confidential because securities legislation in certain provinces requires publication of the written comments received during the comment period. All comments received will be posted on the websites of each of the Alberta Securities Commission at www.albertasecurities.com, the Autorité des marchés financiers at www.lautorite.qc.ca and the Ontario Securities Commission at www.osc.gov.on.ca. Therefore, you should not include personal information directly in comments to be published. It is important that you state on whose behalf you are making the submission.