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May 14, 2014

European Securities and Markets Authority,
103 Rue de Grenelle,
75007 Paris,
France

Via upload to: www.esma.europa.eu

Re: Consultation Paper - ESMA Guidelines On Alternative Performance Measures – ESMA/2014/175

Dear Ladies and Gentlemen:

Standard & Poor's Ratings Services appreciates the opportunity to provide the European Securities and Markets Authority ("ESMA") with comments on its Consultation Paper ESMA/2014/175 "ESMA Guidelines on Alternative Performance Measures" (the "Consultation Paper").

The views expressed in this letter represent those of Standard & Poor's Ratings Services and do not address, nor do we intend them to address, the views of any other affiliate or division of Standard & Poor's Financial Services, LLC or of its parent, McGraw Hill Financial, Inc. We intend our comments to address the analytical needs and expectations of our credit analysts.[1]

Standard & Poor's Supports Efforts To Improve Transparency, Neutrality And Comparability of Alternative Performance Measures (APMs)

We believe the draft guidelines within the Consultation Paper will improve communication by issuers on how they manage their businesses; foster comparability and unbiased financial information; and better enable financial statement users to understand APMs. However, we believe the guidelines could go further to better achieve these aims. We include our views for other potential guidelines in our response to certain questions in the Consultation Paper, which are set out in the appendix to this letter. Some of our suggestions may be deemed broader than the scope of the Consultation Paper but are related to its objectives and are worthy of mention in an effort to help meet financial-statement user needs. To summarize the salient points:

- We support detailed guidelines on alternative *profit* measures, such as those recommendations published by the U.K. Financial Reporting Council (FRC) in

[1] The opinions stated herein are intended to represent Standard & Poor's Ratings Services' views. Our current ratings criteria are not affected by our comments on the Consultation Paper.

December 2013[2] in its reminder to Boards on the need to improve the reporting of additional and exceptional items by companies.

- We believe the finalized guidelines should include standardized definitions for commonly used APMs, such as earnings before interest, taxes, depreciation and amortization (EBITDA). We believe this would enhance consistency and comparability and discourage the potential inappropriate use of APMs.
- We believe that in addition to the requirement to reconcile APMs to the most relevant amount presented in the financial statements, the guidelines should require issuers to provide an explanation as to why management deems it appropriate to remove (or include) each reconciling item to derive the APM.
- We support exploring the idea of auditors providing assurance on APMs. Where such APMs are disclosed, we would prefer them to be incorporated into the financial statements to elevate the level of assurance on the consistency and reliability of the amounts presented. In our opinion, more prescriptive guidance is required for auditors to assist them, in particular, as they scrutinize alternative *profit* measures such as underlying earnings.

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We provide more details to some of the above comments in our responses to certain questions in the Consultation Paper, set out in the appendix to this letter. We also attach our CreditWeek publication of Feb. 26, 2014, which includes several articles giving our perspectives on APMs. We thank you for the opportunity to provide our comments, and we would be pleased to discuss our views with members of ESMA or your staff. If you have any questions or require additional information, please contact the undersigned.

Very truly yours,

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[2] See https://www.frc.org.uk/News-and-Events/FRC-Press/Press/2013/December/FRC-seeks-consistency-in-the-reporting-of-exceptio.aspx.

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<u>Appendix – Standard & Poor's Ratings Services' Responses To Specific Questions In The Consultation Paper</u>

Question 1

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?

We agree.

Question 2

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?

We agree.

Question 3

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.

We agree.

Question 4

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?

Yes, but see additional suggestions in our responses to questions 5-9 and 13.

Question 5

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

We agree the scope of the guidelines should be broad, to include APMs that are relevant to understanding a business. However, we believe it would be helpful for the finalized guidelines to require more detail to explain the circumstances where issuers may not apply all of the principles defined in the guidelines because, in accordance with paragraph 24 of the Consultation Paper, it may not be practicable (when the cost of providing this information outweighs the benefit obtained) or the information provided may not be useful to users. We believe clarification in this area will help financial-statement users understand management's rationale and compare issuer explanations.

Question 6

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

Yes. We also believe the finalized guidelines should include standardized definitions for commonly used APMs, such as EBITDA. We believe this would enhance consistency and comparability and discourage the potential inappropriate use of APMs.

Question 7

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?

We agree the finalized guidelines should include a reconciliation of the APM to the most relevant amount presented in the financial statements. We further support including separate identification and explanation regarding the nature of each reconciling item. We believe the explanation of the reconciliation should include why management deems it appropriate to remove (or include) each reconciling item to derive the APM. For example, if management excludes the amortization of acquired intangible assets from the issuer's adjusted operating profit figure, we would like management to explain why they believe exclusion of this item gives a more relevant depiction of the business performance. In our view, the explanations provided should not be boilerplate but instead tailored to the nature of the issuers' business and the manner in which management deems it applicable to understanding its business.

Question 8

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

We agree. Please also note the answer to question 7 and our recommendation that as part of the explanation and use of APMs, the finalized guidelines should require issuers to explain why they view the APM to be a more relevant depiction of the financial condition, results of operations, and/or cash flows of the business.

Question 9

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?

APMs reported within or outside the financial statements can provide useful information for understanding the financial condition, results of operations, and/or cash flows of the business and can therefore be relevant to analysis. In our view, the APMs should be presented with no more than equal prominence to measures directly stemming from financial statements.

Question 10

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

We agree.

Question 11

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

Yes.

Question 12

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

Yes.

Question 13

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

We believe the draft guidelines, if finalized, will likely improve transparency, neutrality and comparability in financial performance measures for users. However, in our view, the guidelines would go further to better achieve these aims if they captured the following:

- We believe financial statement users would benefit from issuers applying the reminder to Boards published by the FRC with respect to alternative *profit* measures. We support the FRC's recommendations, as follow:

    - The approach taken in identifying additional items that qualify for separate presentation should be even-handed between gains and losses, clearly disclosed and applied consistently from one year to the next.
    - Where the same category of material items recurs each year and in similar amounts (e.g., restructuring costs), companies should consider whether such amounts should be included as part of underlying profit.
    - Where significant items of expense are unlikely to be finalized for a number of years or may subsequently be reversed, the income statement effect of such changes should be similarly identified as additional items in subsequent periods, so readers can track movements regarding these items between periods.
    - The tax effect of additional items should be explained.
    - Material cash amounts related to additional items should be presented clearly in the cash flow statement.

- We support exploring the idea of auditors providing assurance on APMs. Where such APMs are disclosed, we would prefer them to be incorporated into the financial statements to elevate the level of assurance on the consistency and reliability of the amounts presented. In our opinion, more prescriptive guidance is required for auditors to assist them, in particular, as they scrutinize alternative *profit* measures such as EBITDA or underlying earnings.