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Mr Steven Maijoor, Chairman
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ESMA/2014/175

13 May 2014

Dear Mr Maijoor,

Consultation Paper ESMA/2014/175 – ESMA Guidelines on Alternative Performance Measures

We are pleased to respond on behalf of the European Economic Area member firms of Deloitte Touche Tohmatsu Limited to the European Securities and Markets Authority on its Consultation Paper/2014/175 *ESMA Guidelines on Alternative Performance Measures*.

The presentation of Alternative Performance Measures: a global issue that requires cooperation with the IASB and other accounting standard-setters and regulators

The need to address presentation of alternative performance measures (APMs) – sometimes referred to as non-GAAP measures – in various types of communications by issuers to the investors' community is a timely and important issue. APMs can add value to an entity's communication with investors by providing insight into the metrics that management uses to operate the business and, currently, the use and presentation of APMs, whether included inside financial statements or outside, are widespread. However, there is diversity in how these are used and described in Europe, as well as around the world. The lack of guidance in this area and resulting diversity may limit or diminish the usefulness of APMs (or in worst cases lead to confusing or misleading information for users). In that respect, we would support the development of commonly shared guidelines on the presentation of, and related disclosures about, APMs, whose objective would be ensuring the quality, transparency and usefulness of the information provided to users.

We note that debates around the presentation of, and information about, APMs are not just circumscribed to Europe. Several national regulators around the world have taken action on the subject in recent years (e.g. in Australia, in Canada, as well as in Europe). The IFAC PAIB also released, in February 2014, a consultation for a draft International Good Practice Guidance on "*Developing and Reporting Supplementary Financial Measures—Definition, Principles, and Disclosures*". Furthermore, we note that the IASB decided in April 2014 to undertake a research project, as part of the Disclosure Initiative project, on the presentation and disclosure of non-GAAP financial measures within IFRS financial statements[1]. We also understand that there are discussions currently taking place within IOSCO with respect of gathering together, at a global level, regulators' views with respect to the presentation of APMs and related disclosures.

We understand and support the desire of regulators to take the necessary measures to improve and foster clarity in an entity's financial communication to the markets, so as to ensure that when the entity presents APMs, the information provided is useful and not misleading compared to the financial information already required under the applicable accounting frameworks.

We note that APMs are often defined by opposition to "*a measure defined in the applicable financial reporting framework*". However, there is not always a clear understanding of what is "*a measure defined in the applicable financial reporting framework*". We also note that the placement of APMs used by entities could vary. Some may be presented inside financial statements (on the face of the primary statements or in the notes) as well as outside financial statements (e.g. in annual reports, management commentaries, press releases, analyst presentations, etc.), whereas others may be presented outside financial statements only. Accordingly, there is a need for accounting standard-setters, and the IASB in particular, to explain the type of measures that their framework and standards cover and would be acceptable within the financial statements. We suggest that ESMA ask the IASB to undertake this mission as part of the research project mentioned above on non-IFRS financial measures included in financial statements.

In addition, for all the reasons explained above (global nature of the topic, varied placement of APMs in all sorts of documents released to the investors' community – including financial statements, and lack of a clear and common understanding of what is a GAAP measure), we would recommend that ESMA ensures, if it has not done so already, that their proposals are shared with and supported by the IASB and other regulators within IOSCO before any final guidelines are published.

Proposed ESMA's guidelines on APMs

While we agree with many of ESMA's proposals related to the presentation of, and information on, APMs, we believe that some of the principles need to be laid out more clearly before finalisation of the project. In that respect, in order to better understand the guidelines' proposals and their consequences, it would have been helpful if ESMA had explained more thoroughly why the current CESR Recommendation on APMs needs revisiting, what aspects of the CESR Recommendation would be affected and why. We therefore suggest that such explanations are made available at some stage.

Our most significant concerns with ESMA's proposed APM guidelines relate to the scope of documents to which the APM guidelines would apply as well as the type of APMs that would be captured in the proposed scope.

Scope of documents to which the APM guidelines would apply

We consider that the proposed APM guidelines are not sufficiently explicit with respect to the types of documents to which they would apply and how this should be done. As a result, our understanding is that they may apply to a scope of documents larger than those that National Competent Authorities (NCA) would usually review (e.g. analyst presentations, brochures including financial measures, etc.). While we can understand the desire that APM guidelines apply to any document used to communicate with the investors' community, we question how their application could be enforced if the scope of documents to which they apply goes beyond the reach of NCA (or auditors).

[1] Refer to the April 2014 IASB Update

Therefore, we recommend that ESMA should clarify the scope of documents to which the proposed guidelines would apply.

Definition of APMs

If we have understood correctly the types of APMs that would be captured by the proposed APM guidelines, we would consider the scope to be too broad.

We suggest that the guideline on APMs should be limited to the presentation of, and information about, APMs that are financial measures. In addition, the financial measures captured should only be those that have been prepared using financial data underlying the preparation of an entity's historic, current or future financial statements (noting that such data may or may not have been presented in a disaggregated manner in the historic/current financial statements). This is because the primary objective sought is the enhancement of the quality of financial information provided to users. As a result, the APMs that should be of primary focus at this stage should be those that are presented to bring additional relevant information to the users about the understanding of an entity's historic, current or future financial performance.

Other comments

We also have some concerns about the proposed form that the disclosure on APMs should take whenever a document containing regulated information is published, as well as the proposed prominence of the APMs displayed compared to GAAP information. On the former point, we make suggestions thereafter for less burdensome measures. On the latter point, we suggest that a preferable principle is that APMs should not obscure the presentation of, or detract the attention from, GAAP measures.

Finally, we believe that it is essential that users have transparent information on the level of external assurance, if any, attached to APMs presented. This transparency is important, all the more depending on the nature of the APM (historic or prospective data) and placement of the APM (inside or outside financial statements). As a result, we suggest that APM guidelines include disclosure of the level of external assurance, if any, of APMs presented.

We have detailed in the appendix to this letter the above concerns, as well as the elements that we consider important surrounding the presentation of, and disclosure about, APMs.

If you have any questions concerning our comments, please contact Gérard Trémolière at +33 (0)1 40 88 28 21 (gtremoliere@deloitte.fr) or Mireille Berthelot at +33 (0)1 40 88 22 95 (mberthelot@deloitte.fr).

Yours sincerely,

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Appendix

Scope and purpose of the [draft] guidelines

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?

The scope of entities to which ESMA's proposed guidelines on APMs apply is almost the same as the one for the Transparency Directive, and we agree with it. We note that the proposed scope differs from that of the Transparency Directive, in that the Transparency Directive does not exclude States. For clarity sake, we believe that any difference of scope should be clearly identified and explained in the proposed guidelines.

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?

ESMA's proposals with respect to the scope of documents to which the proposed APM guidelines would apply is one of our significant concerns. We consider that such scope is not sufficiently clear and explicit to understand the types of documents to which the proposed APM guidelines would apply.

We observe that the placement of APMs used by entities could vary. Some may be presented inside financial statements (on the face of the primary statements or in the notes) as well as outside financial statements (e.g. in annual reports, management commentary, press releases, analyst presentations, etc.), whereas others may be presented outside financial statements only.

We can appreciate that, as a result, regulators may wish that guidelines on APMs ultimately cover a broad range of documents that an entity uses to communicate with investors, which is not limited to financial statements (e.g. management commentaries, annual reports, press releases, profit warnings, presentations to analysts, prospectus documents, brochures presenting the entity, etc.). This is because we understand, and agree, that expectations in terms of the quality and transparency of financial measures released exist whether they are published in or outside financial statements.

However, where APM guidelines are issued by regulators, questions about compliance reviews and possible enforcement actions necessarily arise. We consider that, if the scope of documents to which APM guidelines apply is too broad, this would create issues around ensuring the completeness of their implementation (including the practical ability to assess compliance with the guidelines in some cases), as well as the possible costs of compliance and enforcement actions. Therefore, it might be appropriate to distinguish clearly how APM guidelines would apply, depending on the types of documents in which APMs are included. For some documents, the guidelines could just be a reference for best practices whereas, for others, there would be expectations that they are followed more specifically.

In Europe, in implementing the Transparency and the Market Abuse Directives, national regulators may have established different scope for the types of documents that might include "regulated information". This contributes to the confusion as to the scope of documents to which the APM guidelines would apply. For instance, would they apply to any document including regulated information such as analyst presentations, brochures and leaflets published by an entity containing financial data, etc.? If so, the proposed APM guidelines would apply to a scope of documents larger than those that National Competent Authorities (NCA) and auditors would usually review. As indicated above, we would question how their application could be verified subsequently in practice. Accordingly, it would be helpful if ESMA clarified and illustrated better the types of documents to which the proposed APM guidelines would apply, as well as how they would apply to them.

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.

As indicated previously, as a matter of principle, we agree that APM guidelines could apply to various sorts of documents, as long as the scope of APMs captured is appropriate (see our comments on Q5) and the way they apply to the documents is clarified (see our comments on Q2).

Prospectuses are one of those documents for which we do not understand why they would be excluded outright from the application of the guidelines. We agree that, as the Prospectus Directive regulates the way certain financial measures should be prepared and presented (e.g. pro-forma information, profits forecasts and some other specific measures), it would be inappropriate to apply the APM guidelines to those specific financial measures. However, if some other financial measures of the nature of an APM are presented in prospectuses, it may be appropriate to apply certain aspects of the APM guidelines to those. To illustrate, whilst we would expect an explanation how the combined or carve-out financial statements have been prepared in a prospectus, several aspect of the proposed APM guidelines (such as reconciliations or prominence) would not be applicable to the measures presented in the combined or carve-out financial statements. However, we consider that, if financial measures such as EBIDTA, other measures of (pro-forma) adjusted profit, or net debt are presented in such documents, it would be appropriate that the relevant principles of the guidelines on APMs apply to them.

Compliance and reporting obligations

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?

As a general comment, it would have been helpful if ESMA had explained more thoroughly why the current CESR Recommendation on APMs needs revisiting, what aspects of the CESR Recommendation would be affected and why. This would have enabled us to better understand the need for ESMA's proposed APM guidelines as well as some of the detailed proposals.

We support the existence of commonly shared guidelines on the presentation of, and information about, APMs, whose objective would be ensuring the quality, transparency and usefulness of the information provided to users, regardless of the placement of APMs used by entities.

We also consider that due to the global nature of the topic, the varied placement of APMs in the various documents released to the investors' community – including financial statements, and the lack of a clear and common understanding of what is a GAAP measure, it is important that ESMA ensures, if it has not done so already, that their proposals are shared with and supported by the IASB and other regulators within IOSCO before any final guidelines are published.

Furthermore, while we agree with many of ESMA's proposals related to the presentation of, and information on, APMs, we believe that some of the principles need to be laid out more clearly before finalisation of the project. In addition, some principles are missing and some may be burdensome to implement, with no demonstration of their particular usefulness. We indicate below our most significant concerns with ESMA's proposals.

[Draft] Guidelines on APMs

Concepts and labels of APMs

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

We find that the definition of an APM is not clear enough to get a common understanding of the boundaries of the application of the guidelines. It seems to us that it is covering a wide-range of measures resulting in the guidelines having too broad a scope. This is a significant concern to us.

First, we note that APMs, or non-GAAP measures in general, are often defined by opposition to "*a measure defined in the applicable financial reporting framework*". However, there is not a clear understanding of what is "*a measure defined in the applicable financial reporting framework*". In particular, to what extent is a subtotal presented on the face of the primary statements in financial statements (e.g. gross margin or operating profit) or additional information presented on such primary statements (e.g. columns distinguishing recurring from non-recurring items) or in the notes (e.g. net debt) an APM? We are also aware of debate about whether figures presented under IFRS 8 are considered to be APMs. The answer to this question affects the acceptability or not to simply reconcile other APMs to the IFRS 8 figures.

IFRSs do not define many financial measures but they give the ability to management to present additional information that they believe to be relevant to the understanding of the financial statements. Does the presentation of this information in financial statements (which may be subsequently used outside financial statements) make it a GAAP measure, or should ESMA's proposed definition of an APM be read restrictively so that any measure that is not clearly defined, or referred to, positively in GAAP is considered to be an APM? We would argue for the latter, to make the application of any proposed guidelines easier to implement.

More generally, we believe that there is a need for standard-setters, and the IASB in particular, to explain the type of measures that their framework and standards cover and would be acceptable in financial statements. The proposed revisions to IAS 1 *Presentation of Financial Statements* under the Disclosure Initiative project, published in March 2014, deal with some issues related to the presentation of subtotals on the face of the balance sheet and statement(s) of profit and loss and other comprehensive income but do not address the issue we raise above in a comprehensive manner. We note that the IASB has decided at its April 2014 meeting to undertake research on the presentation and disclosure of non-IFRS financial measures within financial statements. We suggest that ESMA reaches out to the IASB to obtain clarification about, in short term, what is considered to be an IFRS measure.

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Secondly, the proposed definition of APMs in paragraph 15 and the explanatory paragraphs are confusing as it is not clear whether the proposed APM guidelines would apply to financial measures only or whether they would also extend to non-financial measures. To illustrate our comment, we find the wording in paragraph 15 too general: how close or far the numerical measure shall "*relate to the financial position, comprehensive income or cash flows*" of an entity? It is not also clear how the explanatory paragraph 17 links with and illustrates the definition of an APM as stated in paragraph 15. Paragraph 17 seems to encompass much broader items that do not seem to be contemplated in the principle set out in paragraph 15. In particular, in paragraph 15 of the proposed guidelines, an APM is defined as "*any numerical measure of historical, current or future financial performance, which relates to the* ***financial*** *position, comprehensive income or cash flows, other than a measure defined by the applicable financial reporting framework*". However, the explanatory guidance in paragraph 17 refers to "*additional performance indicators reflecting business activity [...], projection of future cash flows [...] or forward-looking indicators*" without any further reference to the financial nature of the indicator. We read paragraph 17 as explaining that the guidelines apply to performance indicators that may not be just of a financial nature. If our understanding is correct, we would disagree with such a wide scope as its limits would not be well defined. This would render the application of the guidelines' principles difficult, if not impossible.

Another illustration of the difficulty in understanding the application of the proposed definition is highlighted by the discussion in paragraph 19 of the proposed guidelines relating to certain business performance measures, such as sales per square meter. It is unclear whether these are scoped in or out of the proposed guidelines. In our view, they should be scoped out.

We believe that the definition of an APM should focus at this stage primarily on the presentation of, and information about, APMs that are financial measures – and not non-financial measures, such as production or activity levels (e.g. number of bank loans written by a bank, churn rates, hotel room occupancy, etc.). In addition, the financial measures captured should only be those that have been prepared using financial data underlying the preparation of an entity's historic, current and future financial statements (noting that such data may or may not have been presented in a disaggregated manner in the historic/current financial statements). This is because the primary objective sought is the enhancement of the quality of financial information provided to users. As a result, the APMs that should be of focus at this stage should be those that are presented to bring additional relevant information to the users about the understanding of an entity's historic, current or future financial performance.

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?

We consider that the requirement to attach an appendix, including the information on APMs used, whenever an investors' communication includes an APM is very burdensome, with no demonstration of significant benefits. Rather, we believe that some flexibility is needed in deciding the means through which the information (or part thereof) could be made available to users, as long as this information is easily accessible. For instance, in long form documents (e.g. in annual reports), it may not be problematic to include a list including the relevant information on APMs. However, for shorter forms of communication (e.g. press releases, interim financial reporting), a reference to a publicly available list describing the APMs used (e.g. available on the entity's website) could be sufficient, similar to what is proposed in the proposed guidelines for press releases (see paragraph 8).

Reconciliation to amounts presented in the financial statements

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?

We agree that entities should provide a reconciliation to the most relevant GAAP amount presented in financial statements, with an explanation of each *material* reconciling item. However, clarification is required about how to assess what is considered to be "*the most relevant amount presented in the financial statements*".

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

We agree that entities should provide information on the APMs they use, how they are defined and calculated, and why they are considered to provide useful information. We acknowledge that some judgement will have to be exercised in determining the level of descriptions to be made, as the idea is not to increase communication with boiler-plate information. For instance, we might expect less explanation of measures very widely understood and used in the market as opposed to those specific to an entity or less commonly used in the market.

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?

We do not understand why the requirement in paragraph 27 of the proposed guidelines is applicable to APMs presented outside financial statements only. If ESMA believes that the APM guidelines should equally apply to APMs included in financial statements, we believe that ESMA should explain why they would be excluded from the requirement in paragraph 27, as this is counterintuitive.

More generally, the assessment of the prominence of the presentation of an APM compared to GAAP measures may be difficult to make as it could be quite subjective and understood differently (is it a question of font size? placement? other measure?). We are not convinced that the requirement that APMs be displayed with "*less*" prominence than GAAP measures reconciles with the view that APMs can be considered to add value to an entity's communication with investors by providing insight into the metrics that management uses to run the business.

We consider that a preferable principle for the prominence of APMs would be that their presentation should not obscure the presentation of, or detract the attention from, GAAP measures. For instance, we consider that it would be inappropriate if a press release were to describe financial performance including APMs only without also including relevant GAAP measures. In that respect, we note that, in some jurisdictions, the regulator asks that an APM is not presented with "*undue*" prominence compared a comparable GAAP measure.

Furthermore, whilst we can understand the reference to the "*prominence*" and "*emphasis*" of an APM, as stated in paragraph 27 of the proposed guidelines, we are unsure to understand the reference to the "*authority*" of such measure. ESMA should explain these requirements.

Finally, it would be useful if ESMA clarified the type of analysis that would be required to comply with paragraph 29 of the proposed guidelines ("*Should an issuer provide performance analysis using APMs presented outside financial statements, a similar analysis should also be presented using corresponding figures from financial statements again, the latter with greater prominence.*").

Comparability and consistency

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

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

We agree that entities should provide comparative information and explanations about, and the effect of, changes that have been made to the presentation of APMs over time.

We wonder whether the explanation in paragraph 36 of the proposed guidelines would not be better placed as a principle in bold along with those in paragraph 34.

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

We agree.

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.

We agree.

We note that the current CESR Recommendation on APMs includes a specific paragraph reminding that all types of financial information should respect the IFRS-principles for financial statements and in particular the qualitative characteristics of financial information. It would be helpful if the guidelines on APMs would clearly remind this point as well. This could be achieved through an explicit reference to the IASB's Conceptual Framework as regards the qualitative characteristics of useful financial information. For example, paragraph QC4 of that Framework indicates that "*If financial information is to be useful, it must be relevant and faithfully represent what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable*".

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.

No specific comment.

Other comments

Auditors involvement with APMs

We note that the current CESR Recommendation on APMs makes references to the type of work that external auditors provide on APMs. To enable users to assess the confidence they can have in the information provided by entities on APMs, we believe that it is necessary for them to understand the degree of involvement of external auditors with APMs and related information. We suggest that the guidelines require such a disclosure. Of note, we would highlight the difficulty for external auditors if prospective APMs are included in financial statements, as the level of assurance cannot be the same as for financial statements GAAP data. Should ESMA ask for a description of the level of external assurance associated with APMs, we recommend that the guidelines be developed with the input from auditing standard-setters, as well as representatives of the audit profession.