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## Accounting Standards Board launches new financial-performance reporting guidelines

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Canada's accounting-rules setters, troubled by the explosion of customized earnings measures, are launching a project to create new standards to improve the use of alternative measures of profit.

The new initiative, to be announced on Thursday, is designed to also include private companies and non-profits, covering all measures of financial performance. But it can only go so far without the help of the Canadian securities regulators. The regulators, who said last year that they planned formal rules to rein in companies that misuse alternative measures of profit, are the enforcers in the current system. And recent history suggests that guidelines and other voluntary systems may not be enough to solve the problem.

"If we can get dialogue started and get people focused on improving the quality of this other financial information that investors say they're relying on, we think that means people will make better investment decisions because they've got better information," said Linda Mezon, chair of Canada's Accounting Standards Board (AcSB) and the former chief accountant of Royal Bank of Canada. "We didn't see anybody else stepping into this void."

The genesis for the AcSB's "Draft Framework for Reporting Performance Measures" was work by **Veritas Investment Research**, highlighted in a [September, 2016, Globe and Mail article](#) that outlined the widespread use of financial measures that do not conform to generally accepted accounting principles (GAAP). **Veritas** found 70 per cent of the members of the S&P/TSX 60 stock index of large public companies used some form of "non-GAAP" metric in their results as compiled by Bloomberg and many seemed to be violating Ontario Securities Commission guidance on how to report them. An update a year later found an increase in their use.

In February, 2017, the AcSB had a series of private discussions with stock analysts, regulators and other accounting and finance-industry leaders, and found that companies' financial statements, calculated according to International Financial Reporting Standards, made up just a small portion of what people consider when evaluating a company, Ms. Mezon said.

After more discussions, she said, a November AcSB board strategy session resulted in the decision to plow forward with a framework to make the discussion of performance measures more public. "One of my board members said if we're not willing to step up and start this conversation then who? ... Somebody's got to start the conversation."

The OSC and other securities regulators, of course, are on the front lines of this battle. They review the disclosures of the companies whose shares trade on the Toronto Stock Exchange and in other public markets. If something's amiss, they have the dialogue with the company. Once a year, the regulators issue a survey report that highlights concerns they see in Canadian companies' financial reporting.

Much of that, however, occurs in private and is not easily understood by the Canadian investing public. According to Ms. Mezon, "I've had a dialogue with the securities regulators here in Canada and they're concerned because they think we're getting into their space because they regulate the [management's discussion and analysis], they give the guidance on non-GAAP reconciliations. But I say this goes beyond non-GAAP and what we're saying isn't in conflict with what you're saying about non-GAAP, it's supportive."

In a statement to *The Globe*, the Canadian Securities Administration, an umbrella group of regulators, said the framework “will provide non-authoritative guidance on the topic of non-GAAP financial measures. In our view, addressing the quality of disclosure surrounding non-GAAP financial measures and other financial measures is important. Accordingly, the CSA is working on a rule to address this, which reporting issuers will need to comply with once finalized.” The CSA says it anticipates publishing the draft rule this fall.

**Anthony Scilipoti**, chief executive of **Veritas**, said “the important thing is change is apace, and all the standards-setters and regulators understand the importance of this issue, because they recognize financial statements are at the risk of becoming not relevant.”

The framework tries to define what makes a high-quality measure of financial performance – characteristics include relevance, a faithful depiction of performance, comparability, verifiability, timeliness and understandability. And it outlines principles to use that measure, including establishing the policies and governance practices to make it work.

Once the conversation is under way, Ms. Mezon says, “we’d really like to break it down by industry and define a handful of measures and say this is how you’re going to compute them. Users would like us to make it mandatory. We’re not there yet.” Alternately, if there were clear, published standards for calculating and disclosing performance measures, a company that didn’t follow them could be asked by its stakeholders: Why not?

“The Accounting Standards Board is a standards-setter rather than a regulator, so they don’t have enforcement power,” says Richard Talbot, CEO of BristolGate Capital Partners and a former board member of the CFA Society of Toronto. “It’s the securities commissions that would need to do that, so in a way you need a tag-team approach.”

Mr. Talbot said the biggest challenge will be developing sector-specific performance measures for every industry, something the accounting standards-setters have not previously done. “There should be a follow-on process facilitated by the [AcSB], but that is a heavy collaborative effort with the [financial statement] preparers, the investors and the analysts. You’ll get the industry expertise you need around the table so that you can then come up with a set of standards for all industries, with the independence of a standards-setting body, that would then be picked up by the securities commissions, who would require people to follow the standards.”