THE GLOBE AND MAIL

February 14, 2020

Canada’s market cops trying again to police companies’ funny numbers

Bowing to pressure, Canadian securities regulators have scaled back proposed rules designed to rein in companies that use alternative financial measures to make their results look better.

The Canadian Securities Administrators, an umbrella group for all the provincial securities regulators, released its revised rules Thursday after more than a year of feedback. The rewritten rules will cover fewer companies and fewer types of performance measures.

At the same time, the CSA proposal elevates its views from mere guidance, which many Canadian companies have not been following, to formal rules. That will allow provincial securities regulators to pursue enforcement cases against companies they see as having misled shareholders with unduly rosy metrics.

The proposed rules are subject to another 90-day comment period, and regulators hope to publish a final version in the fall. That would allow the rules to take effect next year for companies with Dec. 31 year ends.

“We are quite convinced that we will be achieving our main objective, which is providing clarity and quality non-GAAP performance measures and ratios to investors," said Hugo Lacroix, superintendent of securities markets of Quebec’s Autorité des marchés financiers, which led the project, along with Alberta.

Non-GAAP measures are numbers – often calculations of profit – that deviate from generally accepted accounting principles. The concern is that companies could mislead investors about their true health by crafting their own financial metrics that differ from numbers in their financial statements.

In September, 2018, the CSA rolled out a plan to turn its existing non-GAAP guidelines into rules, with the power of enforcement behind them. That would put Canada on par with the United States, where the Securities and Exchange Commission’s non-GAAP regulations allow it to pursue companies for what it sees as misleading disclosure.

“At the heart of it is the fact that regulators feel that there has been unbalanced disclosure. There has been some abuse, historically,” said Lara Gaede, co-leader of Deloitte’s Securities Centre of Excellence and the former Alberta Securities Commission chief accountant who helped lead the process. “So I think at the heart of the matter is the regulators still fundamentally feel that they need securities law in order to enhance compliance and, when necessary, take enforcement action."

Mr. Lacroix said Thursday that after many reviews of disclosures and comments to companies, Canada’s provincial securities regulators "didn’t feel the needle move to the extent we wanted. We felt we had the right approach, the right guidance. But now, with the rule, it will make our statements stronger.”

The non-GAAP conversation accelerated in Canada in September, 2016, when The Globe and Mail published the results of a report by ***Veritas Investment Research*** that 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 – and many seemed to be violating the CSA's guidance on how to report them.

In an analysis of the 2018 proposal, ***Veritas*** said it "had a much broader scope" than the U.S. rules and expressed concern that companies would provide less information in response. Mr. Lacroix said Thursday that companies indeed said they may cut back on performance measures if they were more tightly regulated.

"We are not saying non-GAAP [measures] should not be used and are not useful," he said. "We think it's important to provide a way for management to put things in context, explain their views and leave to investors the access to that perspective and make their decision."