Thinking About a New or Updated Non-GAAP Financial Measure for COVID-19? Look Before You Leap.

April 17, 2020

The economic disruptions resulting from the ongoing COVID-19 pandemic have had, and likely will continue to have, appreciable economic effects on the business of many companies. One question (among many) companies may consider is whether and how to reflect the impact of COVID-19 in upcoming public disclosure. Indeed, the SEC has specifically requested that companies address investor interest in how the COVID-19 pandemic has impacted company operations and financial condition,[1] and particular focus will be brought to bear on whether and how COVID-related effects have been reflected in non-GAAP financial measures publicly and privately disclosed to investors, lenders and other parties. In unpacking the whether and how regarding non-GAAP financial measures, specific issues to consider include:

- Whether an existing permitted category of adjustments to a current non-GAAP financial measure could accommodate a COVID-19-related adjustment?
- If not, may and should the company create a new permitted category of adjustments to an existing non-GAAP measure, or should the company create and disclose a new non-GAAP financial measure?
- In any case, exactly which COVID-19-related effects may appropriately be reflected as adjustments?

Although relevant considerations will vary by company, the following discussion highlights certain key considerations for evaluating whether and how to reflect COVID-

[1] Statement from Chairman Jay Clayton and William Hinman, "The Importance of Disclosure – For Investors, Markets and Our Fight Against COVID-19" (April 8, 2020) ("April 8 Statement"). https://www.sec.gov/news/public-statement/statement-clayton-hinman.

19-related adjustments in such measures, including U.S. federal securities law, contractual and corporate governance considerations.

U.S. Federal Securities Law Considerations

Avoid Prohibited Non-GAAP Financial Measures

Certain non-GAAP financial measures are *per se* prohibited under SEC guidance:

- **Mind the Limits on Non-GAAP Liquidity Measures**. Cash flow and liquidity measures such as free cash flow are a key focus of companies in light of COVID-19. Given the importance of such measures, keep in mind the following:

  - No Adjustments for Charges or Liabilities That Require Cash Settlement. Non-GAAP liquidity measures generally cannot exclude charges or liabilities that required, or will require, cash settlement (or would have required cash settlement absent an ability to settle in an alternative manner), except for EBIT and EBITDA.[2] Notwithstanding the foregoing, if a material agreement contains a material covenant regarding a non-GAAP liquidity measure that excludes charges required to be cash settled, the company may still disclose such non-GAAP liquidity measure if it is material to an investor's understanding of the company's financial condition and/or liquidity.[3]

  - No Per-Share Non-GAAP Liquidity Measures. The SEC prohibits presenting in documents filed or furnished with the SEC any non-GAAP liquidity metrics which measure cash generated on a per-share basis. The SEC will consider the substance of the non-GAAP financial measure in evaluating whether it is a liquidity measure, even if management characterizes it as a performance measure.[4]

  - Present Three Major Categories of Cash Flows. Given the general prominence requirement to present the most directly comparable GAAP metric (see "Present the Comparable GAAP Measure with Equal or Greater Prominence" below), whenever a non-GAAP liquidity measure is presented, the three major categories

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[2] Regulation S-K Item 10(e)(1)(ii)(A).

[3] Non-GAAP Financial Measures C&DI Question 102.09. If the company discloses a non-GAAP liquidity measure which would otherwise be prohibited by Regulation S-K Item 10(e)(1)(ii)(A), the company should also consider disclosing, in the context of a credit agreement:

- "the material terms of the credit agreement including the covenant;
- the amount or limit required for compliance with the covenant; and
- the actual or reasonably likely effects of compliance or non-compliance with the covenant on the company's financial condition and liquidity."

[4] Non-GAAP Financial Measures C&DI Question 102.05.

of cash flows should also be presented. In light of the strain on liquidity caused by COVID-19, companies disclosing "free cash flow" and other non-GAAP liquidity measures should bear in mind this presentation requirement.

- **Do Not Create Individually Tailored Accounting Principles**. Non-GAAP financial measures that "substitute individually tailored revenue recognition and measurement methods for those of GAAP…[and] other measures that use individually tailored recognition and measurement methods for financial statement line items other than revenue," may be considered misleading.[5] In addition, adjustments for lost revenue could be ripe for challenge given the difficulty of supporting such an adjustment (see "Governance Considerations" below). A company should not adjust a financial metric if any of the following questions can be answered affirmatively:
    - Does the adjustment shift GAAP from an accrual basis to a cash basis?
    - Does the adjustment include transactions that are also reported in another company's financial statements?
    - Does the adjustment reflect part but not all of an accounting concept?
    - Does the adjustment render the measure inconsistent with the economics of a transaction or agreement?[6]
- **Do Not Present Performance Measures "Net of Tax."** The SEC has stated that if "a measure is a performance measure, the registrant should include current and deferred income tax expense commensurate with the non-GAAP measure of profitability…[and] adjustments to arrive at a non-GAAP measure should not be presented 'net of tax'" but should instead be shown "as a separate adjustment and clearly explained."[7]

Present the Comparable GAAP Measure with Equal or Greater Prominence

When presenting a non-GAAP financial measure in a document filed with the SEC or an earnings release furnished to the SEC under Item 2.02 of Form 8-K, the most directly comparable GAAP measure is required to be presented with equal or greater

[5] Non-GAAP Financial Measures C&DI Question 100.04.

[6] AICPA Conference on Current SEC and PCAOB Developments, "Developments in the Division of Corporation Finance" Panel with SEC Deputy Chief Accountant Patrick Gilmore (December 11, 2018).

[7] Non-GAAP Financial Measures C&DI Question 102.11: In contrast, if a measure is a liquidity measure that includes income taxes, the SEC has stated that it might be acceptable to adjust GAAP taxes to show taxes paid in cash.

prominence.[8] In addition, any discussion and analysis of a non-GAAP financial measure, *e.g.*, explaining the effect of COVID-19, requires similar discussion and analysis of the comparable GAAP measure in a location of equal or greater prominence.[9] Given the number of stakeholders involved in drafting earnings release headlines, highlights and quotes from senior officers about financial performance and condition, companies should double check that these disclosures comply with the prominence requirement.

- **SEC Enforcement Action**. In late 2018, the SEC brought an enforcement action and assessed a civil penalty against ADT Inc., finding that ADT violated this requirement in its FY 2017 and Q1 2018 earnings releases (both of which were furnished under Item 2.02 of Form 8-K) by presenting certain non-GAAP measures in the headlines and highlights of the earnings releases without giving equal or greater prominence to the comparable GAAP measures.[10]

Provide a Reconciliation to the Most Directly Comparable GAAP Measure[11]

SEC rules governing the disclosure of non-GAAP measures require the inclusion of a reconciliation of each non-GAAP financial measure to the most directly comparable GAAP financial measure. Such reconciliations must be quantitative for historical non-GAAP financial measures presented and, to the extent available without unreasonable efforts, quantitative for forward-looking information. A stand-alone adjustment for the effects of COVID-19 will generally need to be individually quantified and broken out in the relevant reconciliation. If an adjustment for COVID-19-related effects is incorporated as a further input to an existing non-GAAP adjustment, footnote or other disclosure regarding the adjustment should be updated to indicate the fact of, and, if material, the extent of, the further adjustment for COVID-19. In either case, to the extent an adjusted non-GAAP financial measure is included in securities offering documentation and the COVID-19-related adjustment is not clearly or sufficiently tied to or derived from the books and records of the company, auditors may be unwilling to provide comfort on COVID-19 adjustments and underwriting banks may request that a senior financial officer of the company provide written certification as to the accuracy of the COVID-19-related adjustment.

Recognizing that the effects of COVID-19 may be evolving and difficult to assess in a routine and timely manner, the Division of Corporation Finance of the SEC released

8 As a matter of good practice, the "equal or greater prominence" requirement is generally also observed in connection with the disclosure of non-GAAP measures subject only to Regulation G.

9 Non-GAAP Financial Measures C&DI Question 102.10: The SEC provided as an example of disclosures that would cause a non-GAAP measure to be more prominent: "providing discussion and analysis of a non-GAAP measure without a similar discussion and analysis of the comparable GAAP measure in a location with equal or greater prominence."

10 SEC Enforcement Action 34-84956.

11 Release Nos. 33-8176; 34-47226. Conditions for Use of Non-GAAP Financial Measures (March 28, 2003). https://www.sec.gov/rules/final/33-8176.htm.

guidance related to COVID-19 on March 25, 2020 (the "SEC COVID-19 Guidance"), which provides that, subject to certain conditions, the SEC "would not object to companies reconciling a non-GAAP financial measure to preliminary GAAP results that either include provisional amount(s) based on a reasonable estimate, or a range of reasonably estimable GAAP results" in instances where "a GAAP financial measure is not available at the time of the earnings release because the measure may be impacted by COVID-19-related adjustments that may require additional information and analysis to complete." The conditions set forth in the SEC COVID-19 Guidance are largely consistent with existing requirements under Regulation S-K Item 10(e) and are as follows:

- **Estimates to Which a Non-GAAP Financial Measure Is Reconciled Must Be Reasonable**. The estimate or estimated range of GAAP results "should reflect a reasonable estimate of COVID-19-related charges not yet finalized, such as impairment charges."

- **Non-GAAP Financial Measures Must Not Be Presented More Prominently Than GAAP Measures**. Do not disclose the non-GAAP financial measure "more prominently than the most directly comparable GAAP financial measure or range of GAAP measures" (see "Present the Comparable GAAP Measure with Equal or Greater Prominence" above).

- **Limit the Non-GAAP Measures Reconciled to Estimates to Those Used by Management**. Any non-GAAP financial measures which are reconciled to an estimate or estimated range of GAAP results should be limited to those which are actually being used to report financial results to the Board of Directors. In the SEC COVID-19 Guidance, the SEC reminded companies that it is inappropriate to use non-GAAP financial measures to paint a more favorable picture of the company and that non-GAAP financial measures should be used "for the purpose of sharing with investors how management and the Board are analyzing the current and potential impact of COVID-19 on the company's financial condition and operating results."

- **Explain Why the Reconciliation Is to an Estimate**. To the extent practicable, explain "why the line item(s) or accounting is incomplete, and what additional information or analysis may be needed to complete the accounting."

Importantly and notwithstanding the foregoing accommodation, the SEC COVID-19 Guidance makes clear that "in filings where GAAP financial statements are required, such as filings on Form 10-K or 10-Q, companies should reconcile to GAAP results and not include provisional amounts or a range of estimated results."

Clearly Disclose Why Management Believes the Measure and Adjustment Are Useful

SEC rules governing non-GAAP financial measures included in both filings with the SEC and earnings releases furnished to the SEC under Item 2.02 of Form 8-K require the inclusion of:

- a statement disclosing the reasons why the registrant's management believes that presentation of the non-GAAP financial measure provides useful information to investors regarding the registrant's financial condition and results of operations; and

- to the extent material, a statement disclosing the additional purposes, if any, for which the registrant's management uses the non-GAAP measure that are not otherwise disclosed.[12]

Of recent relevance, the SEC COVID-19 Guidance emphasizes the importance of this requirement, stating, "to the extent a company presents a non-GAAP financial measure or performance metric to adjust for or explain the impact of COVID-19, it would be appropriate to highlight why management finds the measure or metric useful and how it helps investors assess the impact of COVID-19 on the company's financial position and results of operations."

Accurately Characterize and Describe the Adjustment

Whether a company chooses to reflect the effects of COVID-19 on its business by updating an existing adjustment to a non-GAAP financial measure or by creating a new line-item adjustment specifically related to COVID-19, the description of such adjustment should accurately identify the nature of the adjustment so as to not be misleading.

- **Confirm That a "Non-Recurring" Adjustment Really Is Non-Recurring**. The potential duration of COVID-19 is as yet unknown and may be seasonal or continue to impact certain companies for many months to come. Do not adjust a non-GAAP financial measure "to eliminate or smooth items identified as non-recurring, infrequent or unusual, when the nature of the charge or gain is such that it is reasonably likely to recur within two years or there was a similar charge or gain within the prior two years."[13] For clarity, this prohibition relates to the

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12 Regulation S-K Item 10(e)(i) (C) & (D). Disclosure set forth in a Form 8-K *furnished* to (as opposed to *filed* with) the SEC is not subject to the requirements applicable to non-GAAP measures set forth in Regulation S-K Item 10(e). An earnings release *furnished* to the SEC under Item 2.02 of Form 8-K is, nonetheless, required to comply with Item 10(e)(1)(i) of Regulation S-K pursuant to Instruction No. 2 of Form 8-K and, as a result, must include management's explanation as to the utility of the non-GAAP financial measure and satisfy the SEC COVID-19 Guidance. As a matter of good practice, this "management explanation" requirement is generally also observed in connection with the disclosure of non-GAAP measures subject only to Regulation G.

13 Regulation S-K Item 10(e)(1)(ii)(B).

characterization of a specified item as non-recurring when it does not meet the specified criteria. As such, companies may adjust non-GAAP financial measures for recurring items as they deem appropriate as long as they are not characterized as non-recurring, infrequent or unusual.

- SEC Enforcement Action: In an enforcement action against SafeNet, Inc., the SEC brought a claim under Regulation G alleging that the presentation of the company's non-GAAP financial results was materially misleading, in part because the company improperly classified certain integration expenses as "non-recurring" or "one time in nature" although they were, in actuality, ordinary and recurring expenses during the relevant period.

- **Use Clear and Accurate Titles and Descriptions**. If companies adjust a GAAP financial measure to create new non-GAAP financial measures in order to reflect COVID-19-related effects, they should not "use titles or descriptions of non-GAAP financial measures that are the same as, or confusingly similar to, titles or descriptions used for GAAP financial measures."[14] For example, and in particular regarding the measure "free cash flow," the SEC has specifically noted that companies should "avoid inappropriate or potentially misleading inferences about its usefulness" and that "a clear description of how this measure is calculated, as well as the necessary reconciliation, should accompany the measure where it is used."[15] If companies create a new line-item adjustment to a currently disclosed non-GAAP financial measure specifically related to COVID-19, they should avoid designating the line item in a way that may be misleading and/or reflecting non-COVID-19-related adjustments in such newly created line-item adjustment. If companies consider reflecting COVID-19-related effects in a current adjustment to an existing non-GAAP measure, they should consider whether reflecting such effects is consistent with the company's currently existing description of such adjustment and, if not, how to accurately update the description.

Evaluate the Timing and Consistency of the Adjustment

Depending upon a company's particular industry and given the timing of when COVID-19 began to impact various industries and businesses in the United States, a company's quarterly results for the period ended March 31, 2020 may not have been affected to the full extent by the effects of the pandemic. Evaluate whether the upcoming earnings release is the appropriate time to make such adjustment.

- **Avoid Inconsistencies between Periods**. A non-GAAP financial measure can be misleading if it is presented inconsistently between periods. If companies determine

14 Regulation S-K Item 10(e)(1)(ii)(E).
15 Non-GAAP Financial Measures C&DI Question 102.07.

to reflect COVID-19 adjustments to financial measures in their upcoming earnings release, they should disclose the change between periods and explain the reasons for such adjustments as such adjustments will not have been reflected in prior periods. If companies do not reflect COVID-19 adjustments at this time but make COVID-19 adjustments in future periods, or continue to make additional COVID-19 adjustments, "it may be necessary to recast prior measures to conform to the [then] current presentation and place the disclosure in the appropriate context" if the change is significant,[16] particularly if the current and prior periods are presented in direct comparison.

- **Avoid Selective Adjustments**. Avoid making selective adjustments related to COVID-19. Any adjustments that are made should be applied and discussed consistently across similar measures. In addition, companies should be consistent when adjusting for a charge or gain because a non-GAAP financial measure can be misleading if it is adjusted to exclude non-recurring charges without also excluding non-recurring gains that occurred in the same period.[17]

Consider Further Disclosure Required for Changes to "KPIs"

Companies that adjust their financial measures to reflect the impact of COVID-19 may also determine to correspondingly adjust key performance indicators and metrics. On January 30, 2020, the SEC released guidance regarding the Management's Discussion and Analysis of Financial Condition and Results of Operations, explaining that "if a company changes the method by which it calculates or presents the metric from one period to another or otherwise, the company should consider the need to disclose, to the extent material:

- the differences in the way the metric is calculated or presented compared to prior periods,
- the reasons for such changes,
- the effects of any such change on the amounts or other information being disclosed and on amounts or other information previously reported, and
- such other differences in methodology and results that would reasonably be expected to be relevant to an understanding of the company's performance or prospects."[18]

16 Non-GAAP Financial Measures C&DI Question 100.02.
17 Non-GAAP Financial Measures C&DI Question 100.03.
18 Release Nos. 33-10751; 33-88094. Commission Guidance on Management's Discussion and Analysis of Financial Condition and Results of Operations (January 30, 2020). https://www.sec.gov/rules/interp/2020/33-10751.pdf.

In the SEC COVID-19 Guidance, the SEC acknowledged that companies may change how they calculate KPIs as a result of, or present new KPIs related to, COVID-19 and reminded companies to follow the principles set forth in its January 2020 MD&A guidance.

Bear in Mind the Risks of Non-Compliance

In addition to the specific considerations described above, companies should "take a step back" and consider the overall context for any proposed adjustments to a GAAP financial measure or existing non-GAAP financial measure, as well as the associated disclosure, to confirm that such adjustments and disclosure do not contain any material omissions and would not be considered materially misleading. For example, any COVID-19-related adjustment to financial measures should be clearly attributable to a specific impact of COVID-19 on the company's business. Public disclosures regarding non-GAAP measures, whether or not filed, are subject to the anti-fraud provisions of the U.S. federal securities laws, including Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934 and Section 11 or 12 of the Securities Act of 1933.[19] Such liability exposure could include SEC civil enforcement, criminal enforcement by the Department of Justice, private litigation and shareholder derivative suits.

With respect to COVID-19 adjustments to financial measures on a forward-looking basis, senior SEC officials have recently stated that they would not expect to second guess an issuer's good faith attempt to provide appropriately-framed additional forward-looking financial information to its investors and other market participants given the uncertainty in the current business environment.[20] To the extent that COVID-19-related forward looking information is publicly provided (whether non-GAAP or other), companies should take care to avail themselves of the safe-harbors for such statements.[21]

Companies will want to keep in mind that electing not to publicly disclose the impact of COVID-19 can also pose compliance risk. In its April 8, 2020 statement regarding the importance of providing full and fair disclosure during the COVID-19 pandemic, the SEC took the opportunity to remind companies to observe their obligation under Regulation FD to not selectively disclose material non-public information. Referring back to the March 23, 2020 statement from Stephanie Avakian and Steven Peikin, Co-

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19 See Rule 102 of Regulation G, providing that "neither the requirements of Regulation G nor a person's compliance or non-compliance with the requirements of this Regulation [G] shall in itself affect any person's liability under Section 10(b) of the Securities Exchange Act of 1934 or [Rule 10b-5 thereunder]." Furthermore, non-GAAP measures subject to Item 10 of Regulation S-K are subject to potential disclosure liability under the statutory anti-fraud provisions because they are "filed" with the SEC.

20 April 8 Statement.

21 See Section 27A of the Securities Act and Section 21E of the Exchange Act.

Directors of the SEC's Division of Enforcement,[22] the SEC noted that "companies and their investors are well served when [COVID-19-related] information…is held closely until disclosed, and, when disclosed, is broadly disseminated."

Contractual Considerations

Companies considering whether and how to adjust their existing financial measures for COVID-19-related effects should also determine whether contemplated adjustments are permitted under material agreements to which they are party and evaluate the possible consequences of any such adjustment.

Review Credit Agreement and Indenture Terms

It is common for credit agreements to contain maintenance covenants, and credit agreements, "high yield" bond indentures and similar financing documentation to contain negative covenants (subject to exceptions), with such maintenance covenants and covenant exceptions referencing compliance with one or more financial ratios or other metrics. The compliance with or testing of such ratios and metrics often keys off of tailored and specifically defined financial measures such as "Adjusted Net Income" or "Adjusted EBITDA." It may be that these measures, as defined, contain adjustments (including pro forma adjustments) and add-backs that can accommodate adjustments for both COVID-19-related effects as well as initiatives or transactions contemplated in response to COVID-19. These types of measures commonly permit adjustments for extraordinary, unusual or non-recurring items, and pro forma adjustments for "run rate" cost savings, synergies and operating expense reductions. Certain of the terms frequently used to delineate permissible adjustments, such as "extraordinary," were once, but are no longer, defined under U.S. GAAP. Other terms may allow for different and often broader adjustments and add-backs than would be permitted under SEC rules and regulations, such as pro forma adjustments that may reference, but often are not limited in scope to, the types of transactions and pro forma adjustments addressed under Regulation S-X. As such, carefully parsing the wording of these adjustments and any other explanatory or definitional provisions that bear on their applicability is critical in determining whether these types of adjustments are contractually permitted. Depending upon their character, it may also be possible to reflect COVID-19-related effects through other permitted adjustments such as goodwill or other asset impairment charges or losses related to property disruptions or shutdowns. As a general matter, companies should be confident that they have a coherent methodology behind any

[22] "Statement from Stephanie Avakian and Steven Peikin, Co-Directors of the SEC's Division of Enforcement, Regarding Market Integrity" (March 23, 2020). https://www.sec.gov/news/public-statement/statement-enforcement-co-directors-market-integrity.

amounts to be adjusted. Further thought should also be given to the fact that many adjustments or add-backs to these types of financial measures under indentures and credit agreements are two-way streets (*i.e.*, it may be that both gains and losses are required to be reflected). As such, before an add-back or adjustment is made for a COVID-19-related expense, charge or loss, thought should be given to the possibility that a positive swing in a future period would require an analogous reduction. Finally, assuming that a COVID-19-related adjustment is permissible, all financial ratios and other metrics that key off of the relevant adjusted measure should be carefully evaluated to determine whether the adjustment could have unintended consequences under the company's financing or other agreements.

Assess Any Impact on Executive Compensation

Consider the ways in which an adjustment to a financial measure for financial reporting purposes impacts executive compensation. For example, if a financial measure is modified for non-compensatory purposes, will that change carry over automatically into a compensation plan, or does the plan document contain its own definition that may or may not need to be changed? Management and Compensation Committees will need to pay close attention to how adjustments to a financial measure will or will not (and/or should or should not) impact executive pay, as both changes as well as "staying the course" will be appropriate for discussion in future annual proxies, and may also trigger intermediate Form 8-K filings for material changes to compensation plans. Companies will be expected to, and should be able to, defend how the adjusted non-GAAP financial measure still presents a superior metric to a GAAP measure and creates proper long-term incentives. Both the immediate impact and the go-forward impact will need to be assessed and, recognizing that ISS and other shareholder service firms may view these changes as "moving the goal posts," the appropriate level of shareholder outreach and communication should be considered.

The general rules applicable to non-GAAP financial goals in the compensatory context have not changed. Pursuant to Regulation S-K Item 402, disclosure in the Compensation Discussion & Analysis of non-GAAP measure target levels with respect to specific quantitative or qualitative performance factors is not subject to Regulation G or Regulation S-K Item 10(e). However, to the extent a non-GAAP financial measure is presented in the CD&A or elsewhere in a disclosure document for any other purpose, *e.g.*, explaining an adjustment made to such metric as a result of COVID-19 to justify certain levels or amounts of pay, such non-GAAP financial measure is subject to the requirements set forth in Regulation G and Regulation S-K Item 10(e).[23] This is usually done via a cross-reference, and we expect that will continue to be the right approach. However, in light of the unusual circumstances presented by COVID-19, companies should consider whether a more fulsome explanation in the CD&A is appropriate.

[23] Non-GAAP Financial Measures C&DI Question 108.01.

Governance Considerations

Once a company preliminarily determines that it is appropriate and timely to adjust a financial measure for the impact of COVID-19, there are important governance considerations to keep in mind.

Check Internal Policies and Procedures to Ensure Compliance

Review internal policies and/or disclosure controls and procedures governing the preparation and disclosure of non-GAAP financial measures. Adjusting a financial measure may require management to review the appropriateness of such adjustment with, and to obtain the approval of, a disclosure committee, the Audit Committee or both. Even if a company does not have a specific policy related to the preparation and disclosure of non-GAAP financial measures, many Audit Committee charters require review of new and/or adjusted non-GAAP financial measures to enhance the oversight of the use of non-GAAP financial measures, thereby increasing faith in the appropriateness and reliability of such measures. In 2018 remarks, then-SEC Chief Accountant Wesley Bricker noted:

> Audit committees that clearly understand non-GAAP measures presented to the public … are an indicator of a strong compliance and reporting culture. Audit committees can review the metrics to understand how management evaluates performance, whether the metrics are consistently prepared and presented from period to period, and the related disclosure policies. Audit committees that are not engaging in these processes should consider doing so.

Furthermore, to the extent an adjustment is made to a financial measure that is tied to executive compensation (as discussed above), companies should also consult the Compensation Committee for review and approval. Although it may not be strictly required by internal policies, reviewing non-GAAP financial measures with external counsel, accountants and auditors will help to assess the appropriateness of any adjustments.

Maintain Robust Internal Controls

Consider how to measure an adjustment to a financial measure, as well as the related internal controls around the data used. Evaluate whether the new or the adjusted non-GAAP financial measure can be presented consistently and on a timely basis in each period going forward based on reliable data subject to strong internal controls. Formalize and document the calculation of such non-GAAP financial measure, including the reconciliation to GAAP, and establish routine testing to analyze the continued appropriateness of such measures.

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There may be many good reasons to consider adjusting a GAAP financial measure or existing non-GAAP financial measure for the impact of COVID-19 in the near term. That said, it will be well worth spending the time up front to carefully vet such a decision from the many relevant perspectives.

If the addition of a new adjustment to a GAAP financial measure or existing non-GAAP financial measure, or the modification of an existing adjustment to a non-GAAP financial measure, is not permitted or desirable for any of the reasons described above, companies may nonetheless consider disclosing the impact of such item on a stand-alone basis without reference to a GAAP or non-GAAP measure. Note, however, that while such disclosure may not be subject to the federal securities law considerations above regarding the use and presentation of non-GAAP financial measures, it will still be subject to anti-fraud liability under U.S. federal securities laws.

For more information regarding the coronavirus, please visit our Coronavirus Resource Center.

Please do not hesitate to contact us with any questions.

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