

Failure to Present GAAP Measures with “Equal or Greater Prominence” Brings Swift SEC Enforcement Action

January 10, 2019

On December 26, 2018, the SEC settled an enforcement action against ADT Inc. (“ADT”) for failure to comply with the “equal or greater prominence” requirement in Item 10(e) of Regulation S-K. This requirement provides that reporting companies, when presenting a non-GAAP financial measure, must include “with equal or greater prominence” the most directly comparable GAAP financial measure. ADT was ordered to pay a \$100,000 civil penalty and to cease and desist from further violations of Section 13(a) of the Exchange Act and Rule 13a-11 thereunder.

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Specifically, the SEC found that ADT violated the “equal or greater prominence” requirement in its earnings releases for fiscal year 2017 and for the first quarter of 2018 (both furnished under Item 2.02 of Form 8-K) by providing non-GAAP financial measures, such as adjusted EBITDA, adjusted net income and free cash flow, without giving equal or greater prominence to the comparable GAAP financial measures. Furthermore, in the headline of its 2017 year-end earnings release, ADT stated that adjusted EBITDA had increased 8 percent year-over-year, without mentioning ADT’s net income or loss (the comparable GAAP financial measure) in the headline. Similarly, in the headline of its first quarter 2018 earnings release, ADT stated that adjusted EBITDA had increased 7 percent year-over-year, without mentioning ADT’s net income or loss in the headline. ADT also presented in the first quarter release a “highlights” section with bullet points that included non-GAAP financial measures (adjusted EBITDA and adjusted net income) but did not present the comparable GAAP financial measures until later in the release.

The enforcement action against ADT follows a similar action settled in January 2017 against MDC Partners Inc. (“MDC”). Despite undertaking to comply with Item 10(e) in response to an SEC comment letter citing Item 10(e) violations in an earnings release, MDC continued to fail to comply with the “equal or greater prominence” requirement in subsequent releases.

It is worth noting that, as far as the public record indicates, the SEC took its enforcement action against ADT without first engaging with the company through a comment letter, as it did with MDC. Further, ADT had only a relatively short history as a public reporting company, having closed its IPO in January 2018. Given these two

observations, it is likely that the SEC viewed ADT's noncompliance—particularly in the releases' headlines—as a serious violation that required enforcement.

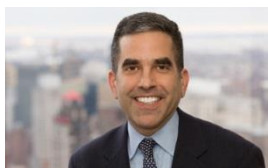
Given the SEC's attention to the use of non-GAAP financial measures in recent years and mindful of the circumstances related to the ADT enforcement action, particularly as we head into the upcoming earnings season, reporting companies should carefully review their use of non-GAAP disclosures for compliance with SEC rules and guidance.

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Please do not hesitate to contact us with any questions.



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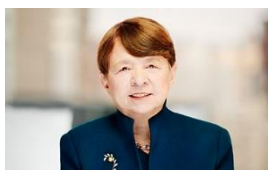
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