

December 5, 2018

BY EMAIL

British Columbia Securities Commission
Alberta Securities Commission
Financial and Consumer Affairs Authority of Saskatchewan
Manitoba Securities Commission
Ontario Securities Commission
Autorité des marchés financiers
Financial and Consumer Services Commission of New Brunswick
Superintendent of Securities, Department of Justice and Public Safety, Prince Edward Island
Nova Scotia Securities Commission
Securities Commission of Newfoundland and Labrador
Registrar of Securities, Northwest Territories
Registrar of Securities, Yukon Territory
Superintendent of Securities, Nunavut

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Me Anne-Marie Beaudoin
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Dear Sirs/Mesdames:

Re: CSA Notice and Request for Comment – Proposed National Instrument 52-112 (“NI 52-112”), Proposed Companion Policy 52-112, Related Proposed Consequential Amendments and Changes (the “Proposed Amendments”)

The Canadian Advocacy Council¹ for Canadian CFA Institute² Societies (the CAC) appreciates the opportunity to provide comments on the Proposed Amendments and respond to the questions posed in the Request for Comment.

¹ The CAC represents more than 15,000 Canadian members of CFA Institute and its 12 Member Societies across Canada. The CAC membership includes portfolio managers, analysts and other investment professionals in Canada who review regulatory, legislative, and standard setting developments affecting investors, investment professionals, and the capital markets in Canada. See the CAC's website at <http://www.cfasociety.org/cac>. Our Code of Ethics and Standards of Professional Conduct can be found at <http://www.cfainstitute.org/ethics/codes/ethics/Pages/index.aspx>.

² CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion of ethical behavior in investment markets and a respected source of knowledge in the global financial community. Our aim is to create an environment where investors' interests come first, markets function at their best, and economies grow. There are more than 154,000 CFA charterholders worldwide in 165+ countries and regions. CFA Institute has eight offices worldwide and there are 151 local member societies. For more information, visit www.cfainstitute.org or follow us on Twitter at @CFAInstitute and on Facebook.com/CFA Institute.

We are supportive of the proposed NI 52-112 and the related consequential amendments and changes aiming to strengthen the disclosure requirements surrounding the use of capital management measures, segment measures and supplementary financial measures, or what others have collectively referred to simply as alternative performance measures or APMs. The proposal creates a set of enforceable standards that will further meaningful disclosures to investors without unduly limiting the ability of an issuer to tell their own story using what it deems to be the appropriate financial measure.

APMs are derived from adjusted GAAP and typically their calculation is highly subjective and not subject to assurance. APMs are a way for companies to report earnings based on whatever logic management finds suitable and the discrepancies between GAAP and non-GAAP earnings can be enormous.³ The reliance on these measures, however, has been progressively increasing among the global investor community. A recent global survey conducted by CFA Institute found that 63% of CFA charterholders thought that APMs should be subject to some regulation.⁴ In fact, the survey revealed the diversity and sophistication of investors' motives for using APMs. Independent, sell side research recently noted that 80% of companies in the S&P TSX60 Index used a non-GAAP measure of net income to adjust and increase the GAAP measure of net income in their securities filings.⁵

The CAC believes the use of APMs is generally reflective of investors' demand for such measures. As CFA Institute research identified, APMs are useful for investors for a variety of reasons, including as a valuation input and as an indicator of earnings quality. Equity investors typically want to translate book values and income statement items into a recurring stream of cash flow or free cash flow ("FCF") as cash flow arguably better reflects the true economic prospects of a business. Additionally, segment measures help investors understand the key valuation drivers for a given business unit (e.g. EV/EBITDA or Price/FCF multiples). APM measures are also used by investors to perform a trend analysis and to adjust for non-recurring items on the income statement (e.g. adjusted earnings per share for non-recurring items). Supplementary financial measures expand upon the information presented in the GAAP financial statements and help investors understand the operating performance of the given business (e.g., growth in same store sales). When compared with the GAAP financial statements, APMs offer a company more flexibility to measure financial performance than GAAP.

According to the Canadian Accounting Standards Board ("AcSB") the primary characteristics of high-quality performance measures are relevance and faithful depiction. Consistency, comparability, verifiability, timeliness and understandability are all

³ <https://www.cfainstitute.org/en/advocacy/issues/non-gaap-reporting>

⁴ CFA Institute, "Alternative Performance Measures –The Latest on Investor Use and Desire for Standardization," *CFA Institute Member Survey Report* (2018), online: <https://www.cfainstitute.org/en/research/survey-reports/alternative-performance-measures>

⁵ Georgopoulos, Taso and Scilipoti, Anthony, "Accounting Alert –Performance Measurement: The Rise of Non-GAAP Metrics," *Veritas Investment Research* (September 8, 2016), online: <https://maximizer.veritascorp.com/virdocs/Accounting-Alert-The-Rise-of-Non-GAAP-Metrics-Veritas-September-8-2016.pdf>

secondary characteristics of high-quality performance measures.⁶ Taken together, these characteristics or principles can help judge the usefulness of a financial measure. From an investor's perspective, a useful measure should either confirm the past value of an entity or help predict the future value of an entity (i.e., the measure should assist in either value realization and/or value creation). The CAC believes that most APMs are useful measures, but they may lack many of the secondary characteristics of a high-quality performance measure such as consistency, comparability and verifiability. The proposed rule will help address such deficiencies by requiring APMs to be more clearly identified, labeled, and reconciled back to GAAP measure along with an explanation for the change in all documents filed with securities regulators.

The CAC agrees with the principles created by the AcSB, and we would encourage the CSA, investors and other standard-setters to collaborate and harmonize any future principles, guidelines or standards that may be applied to the use of or calculation of APMs. Canadian companies compete in and raise capital in a global market and Canada's regulations should therefore position our issuers to succeed on the global stage. A harmonization of standards across Canada and with international standards is ideal.

Investors may benefit from a more transparent, consistent and comparable reporting regime, that includes industry specific APM disclosures. However, we caution regulators not to be overly prescriptive in their approach. Any financial measure that is flexible is also inherently subjective and may be difficult to standardize. Thus, when designing a framework surrounding the use and calculation of APMs, a principles-based approach such as required disclosures and reconciliations may be preferred over a more prescriptive rules-based approach, particularly as it pertains to the calculation of APMs. Any future refinement, beyond what is currently proposed in NI 52-112 should aim to balance investors demand for high-quality disclosures without inhibiting an issuer's ability to communicate the financial condition and prospects of their business or the ability to communicate industry specific measures.

A "comply or explain" regulatory model may help provide investors with the right amount of information without requiring excessive disclosures from issuers. Such a model would require an issuer to report according to a set of enforceable standards or principles, but is also flexible enough to allow an issuer to deviate from such standards when an appropriate explanation is provided. The CAC believes it is possible to reduce the absolute quantity of disclosures while still enhancing the quality of disclosures and promoting investor protection. Requiring excessive disclosure risks overwhelming investors with unnecessary information or worse. In fact, excessive disclosure relating to APMs measures may actually dis-incentivize issuers from communicating fully with their investors and place less emphasis on written materials that are broadly available to investors.

Generally, the CAC suggests that regulators should further embrace the use of data and technology to enhance the utility of disclosures (e.g., investigate further using XBRL

⁶ Linda Mezon, "Canadian Accounting Standards Board – Draft Framework for Reporting Performance Measures" (presentation delivered at the Alternative Performance Measures Working Group, 20 November 2018).

and other similar technologies). We believe that all documents filed with a securities regulator should include detailed reconciliations of any alternative performance measures back to the most representative line item reported under GAAP; however, when APMs measures are utilized in other written documents (e.g. investor presentations), a reference back to the securities filings ought to be sufficient disclosure.

Finally, it is our understanding that many of the requirements in the proposal that requires issuers to identify, label and reconcile APMs are already status quo and were originally established in Staff Notice 52-306. Formalizing the existing Staff Notice into a National Instrument should not be overly burdensome to Canadian issuers. Such formalization of the notice into a rule will also provide regulators with additional enforcement tools if they observe instances of non-compliance. We believe this is a positive step and a useful tool for regulators to possess.

We wish to respond to the specific questions posed as follows.

Responses to Questions listed in the Notice and Request for Comment

1. *Does the proposed definition of a non-GAAP financial measure capture (or fail to capture) specific financial measures that should not (or should) be captured? Please explain using concrete examples.*

No.

2. *Are there any specific additional disclosures not considered in the Proposed Instrument that would significantly improve the overall quality of disclosure and be of benefit to investors? Please explain using concrete examples.*

No.

3. *Is specific content in the Proposed Companion Policy unclear or inconsistent with the Proposed Instrument?*

No.

4. *Is the proposed exemption for SEC foreign issuers appropriate? If not, please explain.*

Yes.

5. *Is the proposed exclusion of oral statements to the application appropriate? If not, please explain.*

Yes, but care should be taken not to dis-incentivize the use of written disclosures in favour of oral disclosure. Written communications are typically more broadly distributed and accessible to investors than oral disclosures (e.g. quarterly financial

statements and press releases are typically more accessible than corporate access meetings and conference calls).

6. *Is the proposed inclusion of all documents to the application appropriate? If not, for which documents should an exclusion be made available? Please explain.*

All documents should not have the same standards apply. For presentation materials where the APMs measure was previously defined, it is sufficient to reference back to the most recent financial statements and reconciliations on file with the securities regulator. For quarterly or annual financial results press releases where full financial statements are posted online concurrently with the press release, a footnoted reference back to the financial statements ought to be sufficient disclosure.

Concluding Remarks

We thank you for the opportunity to provide these comments. We would be happy to address any questions you may have and appreciate the time you are taking to consider our points of view. Please feel free to contact us at cac@cfacanada.org on this or any other issue in future.

This letter is signed jointly by:

“The Canadian Advocacy Council for Canadian CFA Institute Societies”

“Sue Lemon, CFA”

Chief Executive Officer, CFA Society Toronto

“David Smith, CFA”

Chair, CFA Societies Canada