SEC ISSUES CAUTIONARY RELEASE REGARDING THE USE OF "PRO FORMA" FINANCIALS IN EARNINGS RELEASES

On December 4, 2001, the Securities and Exchange Commission (SEC) issued a cautionary release to public companies and other registrants that present to the public their earnings and results of operations on the basis of methodologies other than GAAP. Such presentations are often referred to as "pro forma" financial information.[1] In its release, the SEC emphasized that although "pro forma" financial information can serve useful purposes, under certain circumstances it may mislead investors if it obscures GAAP. The SEC alerted public companies and their advisors to the following:

- First, the SEC issued a reminder that the antifraud provisions of the federal securities laws apply to a company issuing "pro forma" financial information and stated that "companies should be particularly mindful of their obligation not to mislead investors when using this information."

- Second, the SEC explained that particular concerns are raised with the presentation of financial results that (i) address a limited feature of a company's overall financial results[2] or (ii) set forth calculations of financial results on a basis other than GAAP. The SEC stated that such presentations would mislead investors when the basis of the presentation was not clearly disclosed. The SEC cautioned that companies need to be mindful of accurately describing the controlling principles when making such presentations.[3]

- Third, the SEC stated that companies must pay attention to the materiality of the information that is omitted from a "pro forma" presentation, and explained that statements about a company's financial results that are literally true may nonetheless be misleading if they omit material information. For example, the

1 Although the SEC stated that the term "pro forma" has "no defined meaning and no uniform characteristics," it has been generally thought to include accounting, financial and other statements or conclusions based on assumed or anticipated facts.

2 For example, the SEC noted the presentation of earnings before interest, taxes, depreciation and amortization, commonly referred to as "EBITDA."

3 For example, the SEC explained that when a company purports to announce earnings before "'unusual or nonrecurring transactions,' it should describe the particular transactions and the kind of transactions that are omitted and apply the methodology described when presenting purportedly comparable information about other periods."

SEC cautioned that, absent "clear and comprehensible explanations of the nature and size of the omissions," investors will likely be deceived if a company uses "pro forma" presentations to obscure a material result of GAAP financial statements or recast a loss as if it were a profit.

- Fourth, the SEC encouraged public companies to consider and follow the earnings press release guidelines jointly developed by the Financial Executives International (FEI) and National Investors Relations Institute (NIRI) before determining whether to issue "pro forma" results, and before deciding how to structure a proposed "pro forma" statement.[4]

- Fifth, the SEC encouraged investors to compare any "pro forma" financial presentation with the results reported on GAAP-based financials by the same company.

****

If you wish to obtain additional information regarding the SEC release or the FEI/NIRI earnings press release guidelines, please contact the corporate partner who regularly works with you.

Willkie Farr & Gallagher is headquartered at 787 Seventh Avenue, New York, NY 10019-6099. Our telephone number is (212) 728-8000 and our facsimile number is (212) 728-8111. Our web site is located at <www.willkie.com>.

January 8, 2002

---

[4] The FEI/NIRI earnings press release guidelines were published in April 2001. These guidelines address such considerations as scope, timing, content, forward-looking statements and consistency. With respect to "pro forma" results, the guidelines state that "[p]ro forma results should always be accompanied by clearly described reconciliation to GAAP results." In its release, the SEC stated that a "presentation of financial results that is addressed to a limited feature of financial results or that sets forth calculations of financial results on a basis other than GAAP generally will not be deemed to be misleading . . . if the company in the same public statement discloses in plain English how it has deviated from GAAP and the amounts of each of those deviations."