

{ CORPORATE FINANCIAL MANAGEMENT }

# DEVELOPING AND REPORTING SUPPLEMENTARY FINANCIAL MEASURES

Supplementary financial measures are widely used in both internal and external reporting because many senior executives question whether measures developed under GAAP fully capture an organisation's current performance or future prospects.

Examples of supplementary financial measures are EBITDA; underlying profit; and free cash flow. Some commentators believe, however, that organisations use these measures in their external reporting to obscure poor performance.

So the Professional Accountants in Business (PAIB) Committee of the International Federation of Accountants (IFAC) has issued proposed guidance to help accountants measure and report organisational performance.

The proposed guidance, entitled *Developing and Reporting Supplementary Financial Measures*, sets out the principles regarding the qualities a measure should have and the disclosures that should accompany it if it is reported externally.

The guidance is meant for all organisations that want to use supplementary financial measures, regardless of their

size or structure and whether they are private or public. It can also be applied to non-financial measures, such as greenhouse gas emissions or barrels of oil equivalent production.

## Considerations

The guidance builds on the qualitative characteristics of useful financial information as identified in the *Conceptual Framework for Financial Reporting* issued by the IASB and the US FASB. It recommends professional accountants consider a number of attributes when developing and reporting supplementary financial measures. A supplementary financial measure should be:

- ◆ **Relevant** – used by management to assess performance or employed by knowledgeable users of the external report.

- ◆ **Complete** – provides all the information necessary for a user to understand the phenomenon being depicted.

- ◆ **Neutral** – not slanted, weighted or manipulated to obtain a desired result.

- ◆ **Transparent** – aligns with its components and is accompanied by sufficient explanation to make it as free as is practical from uncertainty and estimation error.

- ◆ **Understandable and verifiable** – allows knowledgeable users to understand its construction and limitations, and conclude that it faithfully reports what it purports to depict.

- ◆ **Comparable** – between entities in the same industry and between periods.

- ◆ **Timely** – reported at the same time as the related financial statements.

## Disclosure tips

In addition to these attributes, the guidance provides a number of tips for disclosure of supplementary financial measures:

- ◆ To avoid confusion, supplementary financial measures should be clearly defined. Additionally, the purpose of a measure should be disclosed. Further, supplementary financial measures should be labelled as such and be clearly distinguished from GAAP measures.

- ◆ When the components of a measure change or their calculation changes, the reason for the change should be explained and the comparative amounts should be restated to the new basis of calculation.

- ◆ A supplementary financial measure should include a

quantitative reconciliation of the measure to the most directly comparable reported GAAP measure.

- ◆ A supplementary financial measure should be presented with sufficient information to enable a user to understand its components and see that the measure is complete, neutral and free from error.

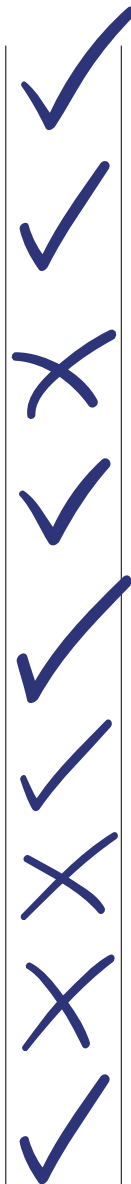
- ◆ An externally reported supplementary financial measure should be presented so that it complements, but does not overshadow, an organisation's GAAP measures.

Given the absence of definitions for supplementary financial measures, many jurisdictions regulate their use and disclosure when reported externally. Accordingly, the proposed guidance should be considered in light of the regulations in the particular jurisdiction where it is applied.

The proposed guidance also includes a limited list of relevant resources from IFAC, its member bodies and other relevant organisations.

## How to comment

The PAIB Committee invites all stakeholders to comment on the proposed guidance by 26 May 2014.



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