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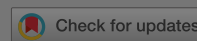
# The Role of Institutional and Economic Factors in the Strategic Use of Non-GAAP Disclosures to Beat Earnings Benchmarks

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## Notes

<sup>1</sup>In the U.S., the December rule (Regulation) became

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<sup>5</sup>An example of the latter is seen in the first enforcement action brought by the SEC pursuant to Regulation G against SafeNet (SEC, [2009](#)). It is alleged that SafeNet represented to investors that ‘non-GAAP earnings results excluded certain non-recurring expenses when, in fact, SafeNet had misclassified and excluded a significant amount of recurring, operating expenses from its non-GAAP earnings results, in order to meet or exceed quarterly EPS targets.’

<sup>6</sup>Analysts’ consensus is defined as I/B/E/S median forecast of earnings per share.

<sup>7</sup>We do not estimate a single logistic regression model of the effect of meeting or beating the earnings benchmark on a non-GAAP basis on the probability of disclosing non-GAAP earnings because this approach would create a mechanical relationship between the dependent and independent variables. Typically, the literature defines benchmark meeting on a non-GAAP basis as an indicator coded as one if non-GAAP earnings meet or beat the benchmark when GAAP earnings fall short. That definition implies that the independent variable in the model is conditional on the firm disclosing a non-GAAP figure. Our approach of estimating two separate models avoids this mechanical relationship.

<sup>8</sup>When more than one non-GAAP earnings measure is disclosed in the same press release we use the first measure as the dependent variable. We also control for this choice in our regression model.

<sup>9</sup>We do not include a control for the firm’s size because larger firms are more likely to have better financial reporting practices (e.g., more GAAP earnings) because they are more likely to be audited by Big 4 auditors. These firms are also more likely to have more GAAP earnings than their non-GAAP earnings. We do not include a control for the firm’s industry because the industry is used in our regression model to control for industry effects. We do not include a control for the firm’s country because the country is used in our regression model to control for country effects. We do not include a control for the firm’s analyst coverage because the analyst coverage is used in our regression model to control for analyst effects.

<sup>10</sup>The adjusted R-squared is used to measure the goodness of fit of the regression model. The adjusted R-squared is used to measure the goodness of fit of the regression model.

<sup>11</sup>We do not include a control for the firm’s size because larger firms are more likely to have better financial reporting practices (e.g., more GAAP earnings) because they are more likely to be audited by Big 4 auditors. These firms are also more likely to have more GAAP earnings than their non-GAAP earnings. We do not include a control for the firm’s industry because the industry is used in our regression model to control for industry effects. We do not include a control for the firm’s country because the country is used in our regression model to control for country effects. We do not include a control for the firm’s analyst coverage because the analyst coverage is used in our regression model to control for analyst effects.

<sup>12</sup>We conducted a number of detailed checks to ensure correctness of the data. We also avoided wire services that transmit shortened or edited versions of press releases, and when non-GAAP information was available from various sources we cross-checked information.

<sup>13</sup>It is important to note that we have collected only non-GAAP measures that portray firms' earnings. Thus, we ignore measures representing other aspects of firms' performance (e.g. sales, cash measures, and financial ratios).

<sup>14</sup>We measure emphasis given to the non-GAAP measures following the six-point scale of Marques ([2010](#)), where 6 stands for 'disclosures in the title of the press release'. This scale is an adaptation of the one originally created by Bowen et al. ([2005](#)). In our sample the average number of non-GAAP earnings disclosed in the same press release is 1.18.

<sup>15</sup>For nonlinear models the accuracy of MEM to measure of the effect of the country factor on the probability of using non-GAAP for benchmark beating depends on the specific value of the country factor. For that reason it is preferable to compute the marginal effect at specific values such as the minimum and the maximum values (Cameron & Trivedi, [2010](#), p. 343).

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