Non-GAAP Reporting following Debt Covenant Violations

I examine two questions: (1) does the transfer of control rights following debt covenant violations affect firms' propensity to provide non-GAAP disclosures? and (2) does the quality of non-GAAP reporting vary following covenant violations?

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- I find that while the frequency of non-GAAP reporting declines following covenant violations, the quality of non-GAAP reporting improves significantly along multiple dimensions. Specifically, when firms decide to report non-GAAP earnings after a covenant violation, the customized performance metric is (1) placed less prominently within the press release, (2) less likely to meet or beat analysts' forecasts when the GAAP number falls short, and (3) marginally less likely to exclude recurring expenses. Moreover, the significant association between non-GAAP exclusions and future GAAP operating earnings disappears following covenant violations, indicating improvement in exclusion quality.
- This study provides the first evidence that debtholders have on an important form of disclosure, non-GAAP reporting.



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	(1) Pr(NGFIRST _t = 1)	(2) Pr(CONSENSU	S _t = 1)	(3) Pr(RECUR _t
/IOLATION ₁₋₁	-0.059**	-0.076***		-0.026
IZE.	(-1.98) 0.001	(-3.32) 0.008		(-0.94) -0.002
	(0.13)	(1.44)		(-0.29)
(TB:	0.001 (1.26)	0.003* (1.94)		0.002 (1.54)
TDROA _t	-0.016	0.099		0.425***
GAAPLOSS,	(-0.19) 0.029**	(1.37) -0.061***		(4.77) 0.021
	(2.26)	(-4.97)		(1.59)
PECIALCHG	0.050*** (4.59)	-0.057*** (-5.34)		-0.140** (-11.88
IEGFE,	0.024**	0.457***		0.063***
OA	(2.46) -0.101	(41.55) -0.160*		(6.53) 0.025
ETURN	(-0.99) -0.009	(-1.68) 0.074***		(0.23)
	(-0.70)	(5.18)		-0.018 (-1.37)
aINST _t	0.008	0.040*		0.009
ANALYST	(0.33) 0.002	(1.80) 0.001		(0.35) 0.002
ITIGATE	(1.46) 0.035*	(1.20) 0.011		(1.52) 0.147***
	(1.66)	(0.52)		(5.55)
iGFIRST ₁₋₁	0.363*** (23.17)			
CONSENSUS ₁₋₁	(23.17)	0.108***		
ECURA		(9.21)		0.251***
				(21.67)
'ovenant Controls ligher-Order Covenant Controls	Yes Yes	Yes Yes		Yes Yes
				Yes
'ear Effects	Yes f covenant violations on	Yes the non-GAAP exclusio		
'ear Effects			n quality (2) FUTGAAP	
ear Effects		the non-GAAP exclusio	(2)	
ear Effects The effect of EPS _{NGa}	f covenant violations on β1	the non-GAAP exclusio (1) FUTGAAP 3.015*** (12.74)	(2) FUTGAAP 3.196*** (13.83)	
EPS _{NO1} × VIOLATION ₁₁	f covenant violations on β1 β2	(1) (1) FUTGAAP 3.015*** (12.74) 3.092 (1.05)	(2) FUTGAAP 3.196***	
ear Effects The effect of EPS _{NGa}	f covenant violations on β1	the non-GAAP exclusio (1) FUTGAAP 3.015*** (12.74) 3.092 (1.05) -0.691***	(2) FUTGAAP 3.196*** (13.83) 3.344	
EPS _{NO1} × VIOLATION ₁₁	f covenant violations on β1 β2	the non-GAAP exclusio (1) RUTGAAP 3.015*** (12,74) 3.092 (1.05), -0.691** (-2.93), 1.207**	(2) FUTGAAP 3.196*** (13.83) 3.344	
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EPS _{NOA} EPS _{NOA} VIOLATION ₅ ,1 TOTALEXCL, TOTALEXCL, BELOWLINE,	f covenant violations on β1 β2 β3 β4 β5	the non-GAAP exclusio (1) RUTGAAP 3.015*** (12,74) 3.092 (1.05), -0.691** (-2.93), 1.207**	(2) FUTGAAP 3.196*** (13.83) 3.344 (1.04) 0.609** (2.09)	
EPS _{N01} × VIOLATION ₈₁ TOTALEXCL, TOTALEXCL, × VIOLATION ₈₁ BELOWINE, SPECIALEXCL	f covenant violations on β1 β2 β3 β4 β5 β6	the non-GAAP exclusio (1) RUTGAAP 3.015*** (12,74) 3.092 (1.05), -0.691** (-2.93), 1.207**	(2) FUTGAAP 3.196*** (13.83) 3.344 (1.04) 0.609** (2.09) -0.019	
EPSxca EPSxca EPSxca × VIOLATIONs1 TOTALEXCL, * VIOLATIONs3 BELOWLINE, SPECIALEXCL, MGRRECUR,	f covenant violations on β1 β2 β3 β4 β5	the non-GAAP exclusio (1) RUTGAAP 3.015*** (12,74) 3.092 (1.05), -0.691** (-2.93), 1.207**	(2) FUTGAAP (13.83) 3.344 (1.04) (1.04) 0.609** (2.09) -0.019 (-0.22) -2.521** (-4.96)	
EPSsoa EPSsoa VIOLATION=1 TOTALEXCL, TOTALEXCL, VIOLATION=1 BELOWLINE, SPECIALEXCL,	f covenant violations on β1 β2 β3 β4 β5 β6	the non-GAAP exclusio (1) RUTGAAP 3.015*** (12,74) 3.092 (1.05), -0.691** (-2.93), 1.207**	(2) FUTGAAP 3.196*** (13.83) 3.344 (1.04) 0.609** (2.09) (-0.19) (-0.21) (-0.22) -2.521*** (-4.96) 0.602	
EPS _{NG8} VIOLATION _{9.1} EPS _{NG8} VIOLATION _{9.1} TOTALEXCL ₄ VIOLATION _{9.3} BELOWLINE, SPECIALEXCL ₁ MGRRECUR,	f covenant violations on β1 β2 β3 β4 β5 β6 β6 β7	the non-GAAP exclusio (1) RUTGAAP 3.015*** (12,74) 3.092 (1.05), -0.691** (-2.93), 1.207**	(2) FUTGAAP 3.196*** (13.83) 3.344 (1.04) 0.609** (2.09) -0.019 (-0.21) (-0.22) -2.521*** (-4.96) 0.602 (0.47) 0.540	
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The effects EPSsca EPSsca EPSsca EPSsca VIOLATION+1 TOTALEXCL, * VIOLATION+1 TOTALEXCL, * VIOLATION+1 BELOWLINE, SPECIALEXCL, * VIOLATION+1 SPECIALEXCL, * VIOLATION+1 SPECIALEXCL, * VIOLATION+1 NGRRECUR, BELOWLINE, * VIOLATION+1 NGRRECUR, BELOWLINE, * VIOLATION+1 NGRRECUR, * VIOLATION+1 Constant Main Controls Covenant Controls Higher-Order Covenant Controls Year Effects Higher-Order Pfects Higher-Order Covenant Controls Year Effects Higher-Order Pfects Higher-Order Covenant Controls Year Effects Higher-Order Pfects Higher-Order Pfe	f covenant violations on βι βι βι βι βι βι βι βι βι	the non-GAAP exclusio (1) BUIGAAP BUIGAAP (1224) (105) (105) (107	(2) PUTGA(3) 3.196 ent 3.1333) 3.334 (1.04) 0.669 ent (2.09) 0.0100 0.0100 0.0100 0.0100 0.0100 0.0100 0.	
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I am in the process of preparing this article for submission to a top accounting journal

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