

SESSION 1: FINANCIAL ACCOUNTING AND REPORTING

DATE: SATURDAY, FEBRUARY 24

TIME: 8:30 – 10:00 AM

**Are Investors Still Misled by *Pro Forma* Earnings
after Financial Reporting Regulations?**

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ABSTRACT: Out of concern that pro forma earnings numbers may mislead the investors, the SEC introduced new rules effective March 2003 to set conditions for the use of non-GAAP measures. We explore whether the pro forma earnings numbers are still misleading after the new rules. In this paper we use a sample of actual pro forma earnings announcements over the period between April 2003 and December 2005 to measure the market reaction to the pro forma earnings and the items excluded from its calculation. We also examine whether there are differences between the behaviors of sophisticated and less sophisticated investors towards the announcements of pro forma earnings. The results do not provide evidence that the market is misled by pro forma earnings. We find no significant difference between sophisticated and unsophisticated investors in terms of their reaction to pro forma earnings. The study provides empirical evidence on the effectiveness of the new regulations.