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SEC Reminds Companies That Earnings Management Can Have MD&A Consequences

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In a settled enforcement action against Under Armour Inc. announced on May 3, 2021 the SEC reminded companies that managing earnings, even if accounted for correctly, can have MD&A implications triggering disclosure obligations. According to the SEC order, Under Armour, in order to meet analyst projections and sustain its 20% quarter over quarter revenue growth record, pressured customers to move purchases forward into the current quarter, and did this for a number of consecutive quarters. There was no finding that Under Armour's accounting for these sales as revenues was improper since the sales were actually made. However, Under Armour gave the same reasons for revenue growth as it had before in earnings releases and its MD&A, without indicating that it was pulling revenues forward to maintain its growth and that this was an unsustainable practice, especially since doing so made it harder to sustain the rate of growth as a result of increasing the prior year's base and taking revenues from the later year.

The SEC charged Under Armour with misleading investors by failing to disclose a key reason for its revenue growth and to identify the significant uncertainty as to whether it would meet its revenue guidance in the future, characterizing this as a "known uncertainty" that indicated that reported results were not indicative of future results and thus had to be disclosed in the MD&A.

The SEC's action against Under Armour underscores the importance of conveying an accurate picture of the drivers of a company's financial results and disclosing known uncertainties concerning its business that could be material to investors.

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