



The Association of  
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June 30, 2014

Mr. Russell Golden, Chairman  
Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, CT 06856-5116

Re: Exposure Draft – Conceptual Framework for Financial Reporting, Chapter 8: Notes to Financial Statements

Dear Mr. Golden:

The Financial Reporting Committee (FRC) and Small Business Financial and Regulatory Affairs Committee (SBFRC) of the Institute of Management Accountants (IMA) are writing to share their views on the Financial Accounting Standards Board's (FASB) Exposure Draft (ED) – Conceptual Framework for Financial Reporting, Chapter 8: Notes to Financial Statements. Descriptions of these Committees can be found in Attachment A of this letter and additional information can be found at [www.imanet.org](http://www.imanet.org) under the Advocacy section.

We are very supportive of the Board's project to develop a conceptual framework for disclosures and agree with the overall objective to improve the effectiveness of financial statement disclosures. The current disclosure landscape is complex and fragmented resulting in uncoordinated and redundant disclosure requirements. We believe a fundamental root cause of this ineffectiveness stems from the lack of a clear disclosure framework. As a result, current disclosures have been designed on a piecemeal basis with inconsistency across and within rule-making bodies. Further, while we agree that user needs are the foundation of effective financial reporting, it seems current disclosure requirements have evolved to address any possible information that might be interesting or even marginally informative to a user versus a holistic assessment of the relevance of the disclosure requirements and the cost and complexity to disclose the information.

Unfortunately, we do not believe that the approach outlined in the ED will result in an operable framework to guide disclosure requirement decision-making. Rather, we believe the approach taken in ED could support almost any conceivable disclosure requirement with no clear guidelines or constraints, because the approach was intentionally designed to be open-ended with an assessment of all possible considerations that may be relevant to disclosure requirements. We see the ED as embracing a "business as usual" approach because it provides very little framework for how the broad range of possible disclosures can or should be narrowed to the most relevant ones and defers such decision-making to the context of individual standard-setting projects. We believe it is just such an approach that has produced the complex requirements that we have today. Accordingly, we fear that this ED will not improve consistency in disclosure requirement decisions across projects and among Board members. We recommend that the Board develop guidelines that it would use to filter potentially relevant disclosures down to the most relevant disclosures so that the proposed disclosure framework will facilitate an effective and balanced set of disclosures. We believe including only the considerations of the relevant disclosures, as the ED does, is not sufficient. As it currently stands, we



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do not view the ED as providing a conceptual framework that, like the other concepts statements developed by the Board, “set forth objectives and fundamentals that will be the basis for development of financial accounting and reporting standards.”

Once such a filtering approach is developed, we recommend that the Board conduct field tests to assess whether the framework provides an actionable resource to guide disclosure requirement decision-making. We believe fair value measurements, pension/OPEB and income taxes would be compelling topics for field testing a revised disclosure framework. The FRC and SBFRC welcome the opportunity to participate in field testing to assist the Board in the development of the disclosure framework.

Our key observations and recommendations follow.

### Framework Design

We agree with the “mission statement” summarized in paragraphs S2 of the ED – that is, that the notes should supplement and further explain information in the financial statements. However, we believe the ED and Appendix A appear to span beyond that “mission statement”. As noted above, as stated in paragraphs P13-14, the Board’s approach intentionally provides for a broad range of possible disclosures and provides very little framework for how it will narrow these possibilities to the most relevant ones, deferring such decision-making to individual standard-setting projects, which is effectively the approach the Board applies today. The ED is a framework that is designed to be comprehensive of all possible considerations. We believe this approach is inconsistent with the development of a framework that would help drive coordinated and consistent decisions on disclosure requirements. As a result, we do not believe the proposed model will lead to clear guidelines for possible disclosure requirements.

We believe the ED should contain not only a framework to identify broad range of potential disclosures, but also a framework to narrow those potential items down to the most relevant set of disclosures. As part of that framework, we recommend that potential disclosure requirements be subject to robust user relevance (what specifically would a user do with the information?), as well as assessments of the cost and complexity of compiling that information. Questions similar to those included in the Private Company Decision Making Framework regarding relevance to users and cost and complexity are appropriate to ask in the context of the Disclosure Framework. In the private company framework, paragraph 1.2 states that the framework used by the FASB must result in disclosure requirements that provide relevant information to users of financial statements at a reasonable cost.

Appendix A of the ED identifies over 50 considerations for disclosure with no guiding hierarchy or constraints on how the Board would incorporate those considerations in developing disclosures for a project. Absent some hierarchy or constraint, we believe this long list of considerations could be used to support almost any disclosure and, if not limited in application, could result in significantly more disclosures in the future. Further, we view a number of the considerations as incremental to current disclosure requirements. Paragraph D38 identifies information that will be useful for **some line items in some circumstances**. We struggle to understand how the Board will apply this concept in future standards. In particular, the considerations included in paragraph D38d, are open-ended and of the type



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that are generally considered for inclusion in forward-looking risk factor disclosures. Similarly, paragraph D58 introduces a disclosure requirement threshold for information that **might be decision useful**, which introduces a very low threshold to initiate disclosure requirement decisions.

We support a decision model that introduces selective criteria and results in some minimum level of suggested or required disclosure menus for each topic and believe such a model deserves more study. Open-ended disclosure models are not operational in the legal and regulatory environment of the United States.

### Financial Statement Line Items

One of the considerations in the ED addresses providing further information about financial statement line items. We recommend that the approach be modified to focus on broader transaction flows, versus individual financial statement line items. This recommendation is consistent with the FASB's standard-setting agenda that is oriented across transaction flows (i.e., revenue recognition, leases, share-based compensation), not specific financial statement line items. We accept that disclosures may be necessary for individual financial statement line items. However, we believe the relevance of disclosure requirements can be better assessed at the broader transaction flow level.

### Materiality

Paragraph D18 states "the Board should establish requirements that are not so prescriptive that they preclude reporting entities from making materiality judgments." However, the ED does not discuss how the Board thinks a reporting entity would apply the concept of materiality. Paragraph D37 states "ultimately each line item should be explained in enough detail for a user to understand the nature of the underlying phenomenon and significant uncertainties, if any, about ownership, obligation or other matters that the entity considered in determining whether to recognize the item."

We accept that preparers are best positioned to make materiality conclusions with respect to entity-specific disclosures. However, we believe the ED should also include a materiality framework for consideration, either specifically in the decision questions or in an expanded cost constraint (cost/benefit) section. The framework should give explicit considerations to the importance of matters to users. If some matters are not important to users, the disclosure framework should eliminate such matters from the decision process. The ED's approach seems to place the entire burden on preparers who, when faced with the challenge of auditor and regulator (including the PCAOB) second-guessing, err on the side of full disclosure of all items, irrespective of relevance.

We suggest that the FASB coordinate with the IASB on its Disclosure Initiative, particularly with respect to materiality.

### Cost-Benefit Assessment

We believe the ED's cost constraint concept in paragraphs D19-21 is too narrow. The cost constraints in the ED address the utility in the context of information that is broadly available from other sources and information regarding general conditions. There is nothing in the ED that addresses how the Board



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will assess the relative value of information that is particular to an entity and not available from other sources (and how that information will be used by current and potential investors) as compared to the costs and complexity of compiling that information in deciding what disclosures it will require. We believe the utility of the information to investors and the cost for preparers to collect and disclose the financial information should be additional elements of the cost constraint assessment. This would provide a more robust assessment of preparer cost against the relevance of the data to guide disclosure decision-making. We believe that there should be a rebuttable presumption to exclude readily available information and information not used by management in operating the entity.

#### Limitation on Information that May Have Negative Economic Consequences

We are supportive of the ED's principle in paragraph D31 that disclosures of expectations and assumptions about the future that are not inputs to current measures in financial statements or notes should be excluded.

The ED is not clear on how the criteria in paragraphs D27-29 would limit the disclosure of the information requested by Question L6 in Appendix A. Specifically, it is not clear which of those paragraphs applies to the information requested by Question L6. We also struggle with how the Board would decide when a company's plans should be disclosed and whether it would differentiate between plans that are subject to external factors and plans that are not. In our experience, almost every plan is subject to external factors that are outside of the reporting entity's control.

#### Information Content of Notes to Financial Statements

While certain considerations and elements addressed in paragraphs D32-57 may be relevant, we have the following significant concerns about some key elements in this section.

- We do not believe the considerations in paragraph D38d provide more perspective on recorded balances, but rather on underlying business trends and potential implications to future trends. Such information is forward-looking in nature and more appropriately addressed in MD&A which is covered by safe harbor rules for public entities and available from management for private entities.
- We do not believe the information in paragraph D44 is particularly relevant in the context of footnotes. For public companies, general information about the entity and its activities are already fully disclosed in periodic filings. For private companies, investors have more direct access to management, and as result, should have other means to access that information.
- We strongly object to the premise that much of the information of the nature addressed in paragraph D57 should be considered for inclusion in the footnotes. Much of the information covered by this section, in particular the information discussed in b, c, d and portions of e, is forward looking and deals with risks that impact future operations, trends and risks. Such information does not provide perspective on recorded balances and is much more appropriately disclosed in the context of MD&A and risk factors of public filings. As noted, investors have access to management of private companies for such information.



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We acknowledge that our views in the above bullet points are colored by disclosures already required for public companies and the Board needs to consider all entities that follow US GAAP. If the Board believes similar disclosures are required for non-public companies, we believe that need can be best addressed through the PCC, considering such disclosures for public companies introduces redundancies and significantly impacts legal exposure due to safe harbor differences between footnotes and other sections of SEC filings. Alternatively, the Board could add a project similar to the IASB's project on Management Commentary. Since public companies already provide "management commentary" in the form of MD&A, the Board's concerns (discussed in paragraph BC6) about investors not having access to information about operational risks only apply to private companies.

### Interim Financial Reporting

We believe that interim reporting is the area most in need of change in the current reporting environment. In the ED, we see some hopeful signs that the framework will recognize the differences between interim and annual reporting, but we are concerned that paragraphs D69 and D70 leave the door open for continued expansion of disclosures in interim filings.

Our specific comments on the draft principles follow.

- We believe that this section should begin with paragraph D61. We would add the notion that interim statements are intended to be "condensed", which refers not only to the length of the footnotes but also to the degree of line item detail in the core financial statements (paragraph D71 alludes to the level of aggregation but is unclear on this point). We do not believe that paragraph D60 is necessary as a free-standing paragraph (D61 explains why interim reporting is different) but the point that interim statements have unique characteristics and limitations is helpful in augmenting the premise of D61.
- We believe that there is an important investor benefit from the concept of interim statements as an update of annual statements, namely that they can more easily identify new information and meaningful changes from the last annual set of financial statements. For example, paragraph D67 notes that contingent liabilities may have highly uncertain outcomes and so should be included in interim filings. This suggests that companies include their contingency disclosures in their entirety in their interim filings. We believe that investors would prefer to know about relevant changes from the latest annual filing with no disclosure in interim reporting if there has not been any material developments. If this is not done, they will need to compare the annual and interim contingency disclosures to determine whether there has been a change, and if so, what those changes were.
- Continuing with this theme, we believe there should be a high hurdle for mandating new recurring disclosures in interim filings that would not otherwise be necessary to update investors on changes. In this regard, we believe that condensed versions of annual segment and revenue disclosures should be the only disclosures included in interim reports without consideration of the degree of change from annual amounts. All other disclosures should be subject to the thought process articulated in paragraph D66.



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Overall, we believe it would be helpful to specifically acknowledge the practical realities of providing timely updates of annual financial statements in interim filings. Interim reporting cycles are so compressed that further expansion of disclosure requirements puts enormous pressure on the timeline for releasing the information to investors. It is, therefore, imperative that the Board is very cautious in determining when, if at all, a disclosure should be required to both annual and interim filings. We do not get that sense from the way that the interim reporting segment of the ED is written.

### Coordination with Other Regulatory Bodies

We are encouraged by the growing consensus that disclosure effectiveness should be addressed. We are also pleased that the SEC and FASB staffs have been in contact throughout the course of the project. The stars are aligning to address this topic. We believe an integrated approach among the SEC and FASB staffs is essential to deliver a meaningful change in disclosure effectiveness.

We are disappointed to see little progress to clarify the disclosure boundary between financial statements and MD&A. In some respects, the ED blurs the boundary further, as evidenced by our comments on paragraphs D32-57 above. Such conditions and circumstances are not part of the historical, factual information under the purview of the FASB.

We accept that there is much an investor might like to know that goes beyond historic financial reporting. However, historical financial statements and footnotes are just one data element utilized by investors. We fundamentally believe that the primary financial statements and footnotes should focus on the “what.” The “what if” and “why” should be addressed in MD&A. We believe that a failure to scale back the disclosure scope and threshold will result in companies and auditors adopting full compliance with all requirements, regardless of relevance.

We believe clarification and coordination of the disclosure boundary between the financial statements and MD&A will meaningfully improve disclosure effectiveness. We would welcome any opportunity to support this coordination.

### Field Test Recommendation

We recommend that the Board conduct field tests to assess whether this ED (or preferably a revised ED that addresses some of the concerns expressed herein) is an actionable resource to guide disclosure requirement decision-making. We propose fair value measurements, pension/OPEB and income taxes as compelling disclosure topics for field testing. The field testing should be initiated by FASB application of current disclosure requirements with the framework to assess the operability of the framework. The conclusions could then be shared with preparers, auditors and users to define how to develop selection criteria for disclosure requirements that balance relevance with cost and complexity. Such criteria could then form the basis of a disclosure framework that can be leveraged for future standards. The FRC and SBFRC welcome the opportunity to participate in any field testing to assist the Board in the development of such criteria.

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Should you have any questions, please do not hesitate to contact us.

Sincerely,

A handwritten signature in blue ink, appearing to read "N. Schroeder".

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A handwritten signature in blue ink, appearing to read "J. Exline".

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## **Attachment A**

### **Financial Reporting Committee**

The FRC is the financial reporting technical committee of the IMA. The committee includes preparers of financial statements for some of the largest companies in the world, representatives from the world's largest accounting firms, valuation experts, accounting consultants, academics and analysts. The FRC reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations.

### **Small Business Financial and Regulatory Affairs Committee**

The SBFRC addresses issues that impact small and medium-sized organizations on behalf of IMA members. The SBFRC engages and suggests solutions to standard-setters and regulatory agencies such as the FASB, SEC, International Accounting Standards Board, Small Business Administration, American Banker's Association, Internal Revenue Service and others.