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Technical Director, File Reference No. 2015-300
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Piercy Bowler Taylor & Kern (PBTK), Certified Public Accountants and Business Advisors, is a regional PCAOB registered accounting firm with offices in Las Vegas, Nevada, and Salt Lake City, Utah. We are pleased to comment on the Board's Exposure Draft (ED) dated September 24, 2015, entitled *Proposed Amendments to Statement of Financial Accounting Concepts No. 8, Conceptual Framework for Financial Reporting, Chapter 3: Qualitative Characteristics of Useful Financial Information.*

The ED was issued concurrently with, and is integrally related to, the prospective amendment to the FASB's *Accounting Standards Codification* contained in its proposed Accounting Standards Update (which we view as more significant than this proposal) entitled *Notes to Financial Statements (Topic 235) Assessing Whether Disclosures Are Material* (File No. 2015-310). Accordingly, despite some limited but necessary redundancies, this letter should be read in conjunction with our more specific comments contained in our accompanying letter on the other proposal.

For your information, both proposals are generally consistent with the views expressed in an article entitled "Finding the Forest Among the Trees: Overcoming Overload and Achieving Greater Disclosure Effectiveness,"[1] authored by the undersigned and published in July 2015 by the New York State Society of CPAs in *The CPA Journal*.

In this ED (File 2015-300), the Board presented only one question to be addressed by respondents, *i.e.*, "*Do the proposed amendments improve Concepts Statement 8? If so, how? If not, why?*" Our response follows.

It is our view that the Board's recognition in its Conceptual Framework that materiality is a legal, rather than an accounting, concept, represents a welcome improvement to its body of literature.[2] This is particularly true in view of the significant difference between its current definition in Chapter 3 of its *Statement of Financial Accounting Concepts No. 8* (CON 8) and the one embodied in the decision of the U.S. Supreme Court in *TSC Industries, Inc. v. Northway. Inc.*, 426 U.S. 438, 449–450 (1976), which was reaffirmed in *Basic Inc. v. Levinson*, 485 U.S. 224 (1988), and subsequently adopted as part of §10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5. In substance, this difference is the difference between "could" and "would" with respect to the probability of influencing the decisions of investors and potential investors and, accordingly, is (theoretically) a higher threshold than the current definition affords.

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1 https://www.nysscpa.org/news/publications/the-cpa-journal/article-preview?ArticleID=9750#sthash.PxWSKeCA.dpbs.

2 However, we do see a possible practical problem with this in the context of auditor communications with lawyers, which is discussed in our response to Question 9 (***Q9***) in the accompanying letter on File No. 2015-310.

It should be noted that in its 1976 decision, the Supreme Court limited its "definition" of *material* to omissions of factual information (*i.e.*, disclosures); it was not extended to misstatements as paraphrased and therefore implied in the proposed amendment of paragraph QC 11 in the ED. However, the definition was effectively expanded to cover misrepresentations of fact in the Court's 1988 decision and has come to be applied generally with regard to both. disclosure misstatements and matters of measurement, as well. We further believe that the words, "in the context of the antifraud provisions of the U.S. securities laws," should be deleted from the final amended paragraph QC 11 since they are misleading in that they erroneously imply applicability only to SEC issuers. We understand that the 1976 Supreme Court decision is, in fact, the "law of the land," and is, therefore, applicable to all preparers of financial statements.

We also believe proposed amended paragraph QC 11 should be modified in its final version because its second sentence (which reads "In the United States, a legal concept may be established or changed through legislative, executive, or judicial action") gives a misleading impression that the operative legal definition is a rapidly moving target likely to change in the near term and, therefore, requires careful monitoring in multiple jurisdictions by financial statement preparers and their auditors. In fact, as noted in the preceding paragraph, the Supreme Court definition is the controlling "law of the land," it has been for 39 years, and it is not likely to change at any time soon.

Also, although it would appear on the surface that the definition embedded in the 1976 Supreme Court decision affords a higher threshold for setting materiality than the more restrictive, extant CON 8 definition, both are highly subjective, and accordingly, neither affords financial statement preparers or their auditors much help in making materiality judgments. Therefore, in our opinion, the proposal in the ED will not likely have much impact on the day-to-day materiality judgments of preparers or auditors. Nevertheless, we see the proposed removal of the FASB's current definition from CON 8 as having the substantial benefit to both preparers and auditors of mitigating their exposure to liability[3] or other adverse consequences of a legal or regulatory challenge to such judgments when made diligently and in good faith. In short, we believe adopting the essence of this proposal will make materiality judgments considerably more defensible.

Under the 1976 Supreme Court definition, a plaintiff would have the burden of proving, not only that an omission (or misstatement) of information, in fact, influenced an investment decision that caused the plaintiff damages, but also that it was reasonable to have expected that such omission ***would***, as opposed to ***could***, have such influence as under the FASB's extant definition. The Court's definition presents a substantially higher plaintiff's burden of proof. We like that.

A more significant feature of this proposal, we believe, even than the foregoing, is the FASB's clearer and more emphatic disclaimer of responsibility to define or prejudge materiality and its implied related acknowledgment (which we would prefer be more clearly articulated) that materiality judgments (as would be guided by the currently operative legal definition) are the responsibility of management of the reporting entity. We regret that many do not seem to understand that, since the purpose of the FASB concept statements is to guide the Board in developing future standards that are consistent with their basic underlying constructs, and not to guide financial statement preparers and auditors in the application of such principles, the concept statements are not to be regarded as authoritative sources of generally accepted accounting principles. This clarification, at least with respect to materiality guidance, should help prevent financial statement preparers, auditors, regulators, litigants and adjudicators from inappropriately looking to nonauthoritative FASB literature for a definition and should redirect their attention appropriately to the Supreme Court decision.

Thank you for the opportunity to comment on this ED. We hope the FASB staff and the Board will consider our views and find them useful in their deliberations on these issues. We acknowledge our awareness that the Board will make our comments publicly available online.

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[3] As we note in our letter regarding File No. 2015-310, one cannot protect oneself against litigation risk, since anyone can sue most anybody for anything, but protection from exposure to liability can be obtained.

Any questions about our comments may be directed to the undersigned at 702/384-1120 or hlevy@pbtk.com.

Very truly yours,

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