

December 6, 2015

Mary Jo White/Chair  
James Schnurr/Office of Chief Accountant  
Securities and Exchange Commission

Members  
Financial Accounting Standards Board

Via email

[director@fasb.org](mailto:director@fasb.org)

[rule-comments@sec.gov](mailto:rule-comments@sec.gov)

Re: "Materiality," File Reference No. 2015-310

We, the undersigned, express our strong opposition to the proposed concept release and notes to financial statements on Topic 235 regarding materiality.

Congress declared that the Securities Exchange Commission would administer disclosures and referee such issues as the definition of materiality.<sup>1</sup> To inform its decisions, the SEC looks to the Financial Accounting Standards Board (FASB). FASB represents itself as a respected repository of thoughtful experts.<sup>2</sup> Because the SEC may ignore FASB's initiatives, FASB presumably engages in iterative conversation with SEC officials as it proceeds to ensure acceptance of its standards and guidelines.<sup>3</sup> We believe what this means in practice is that what FASB

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<sup>1</sup> [http://www.huffingtonpost.com/barbara-roper/sec-turns-disclosure-into\\_b\\_8462482.html](http://www.huffingtonpost.com/barbara-roper/sec-turns-disclosure-into_b_8462482.html)--Bulletin 99, Materiality, SEC (1999), available at: <https://www.sec.gov/interps/account/sab99.htm>

<sup>2</sup> On its website, FASB explains: "The FASB accomplishes its mission through a comprehensive and independent process that encourages broad participation, objectively considers all stakeholder views, and is subject to oversight by the Financial Accounting Foundation's Board of Trustees." See <http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1351027215692>

<sup>3</sup> Tom Selling, a professor and former SEC staffer with the Office of Chief Accountant, explains, "The probability that [SEC Chief Accountant James] Schnurr isn't fully supportive of the FASB proposals is essentially zero. Hence, it strains credibility that Mr. Schnurr didn't provide at least some initial direction to the FASB. Otherwise, why would the FASB want to be sticking its nose in the PCAOB's business?" The Accounting Onion, by Tom Selling (2015), available at: [available at: http://accountingonion.com/2015/10/fasbs-proposed-materiality-clarifications-are-backfiring.html](http://accountingonion.com/2015/10/fasbs-proposed-materiality-clarifications-are-backfiring.html)

promulgates carries the implicit imprimatur of the SEC. Consequently, our comment to FASB is also a comment to the SEC, as we view the institutions as collegial.

Currently, as described by the FASB, materiality means information that “could” influence investor decisions. Materiality applies to the notes in a financial statement, namely, the descriptive deconstruction by management of specific items that are part of the aggregate quantifications in the financial statement (either the income statement or balance sheet).<sup>4</sup>

Comes now a proposal to change the definition of materiality from what “could” influence an investor, to what “would” influence the investor.

FASB explains that this new description of materiality stems from a long-term FASB “project” titled “Disclosure Framework.” FASB states that the “Board hopes that a sharper focus on important information will result in reduced volume in most cases.”<sup>5</sup> We disagree with this goal. In general, more disclosure is better than less disclosure.<sup>6</sup> Finance-based problems stem from a lack of disclosure, from “reduced volume,” such as Enron, World Com, the Madoff Ponzi scheme and many others. The 2008 financial crisis depended on material risk masked from investors.

As to the claim that investors suffer from information overload, we need only point to such devices as search engines on computers, and the availability of Wall Street industry analysts who can cut through the chaff of corporate reports. We are unaware of any groundswell of investors petitioning the SEC for less information.

We are concerned that FASB adopted its goal of winnowing corporate reports with the help of and because of those it recruited to advise it. FASB explains that its “Disclosure Framework” project results from the advice of a “resource group.”<sup>7</sup> This resource group generally decided that information that “could be useful to investors ...” was considered too broad and too low a

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<sup>4</sup> One imagines that the accounting industry might have developed a manual that establishes numerical metrics. The question of materiality is undoubtedly informed by the hundreds of independent auditor hours expended each year at many thousands of public companies, a ritual that has taken place for many decades. Further, the stock market provides a minute-by-minute evaluation of information that changes stock prices. Given this one might hope that a concept so basic as materiality would enjoy a more muscular description than what seems little beyond a tautology, namely, that which could change an investor’s view.

<sup>5</sup> See FASB Project Update, (website visited October 2015), Available at: [http://www.fasb.org/cs/ContentServer?c=FASBContent\\_C&pagename=FASB%2FFASBContent\\_C%2FProjectUpdatePage&cid=1176156344894](http://www.fasb.org/cs/ContentServer?c=FASBContent_C&pagename=FASB%2FFASBContent_C%2FProjectUpdatePage&cid=1176156344894)

<sup>6</sup> See press release, Univ of Tennessee, available at: <http://tntoday.utk.edu/2015/10/29/carcello-speaks-proposed-rules-limiting-disclosure/>

<sup>7</sup> FASB Resource group: [http://www.fasb.org/cs/ContentServer?c=Document\\_C&pagename=FASB%2FDocument\\_C%2FDocumentPage&cid=1176160567809](http://www.fasb.org/cs/ContentServer?c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176160567809)

threshold. Participants generally favored using “would be useful” instead of “could be useful.” Who were these participants? Not one of them could be described primarily as an investor, or consumers of material information.<sup>8</sup>

We believe the proposed change by FASB threatens serious harm. FASB’s proposed change would lead to less disclosure of material information in two important ways. First, it devalues the standard of information from what “could” influence a capital provider, to information that would “substantially alter” the views of the capital provider. By itself, this higher hurdle will mean that some information currently described in the notes will now go missing.

Second, FASB declares that the concept of materiality is a legal concept. A legal concept is one that can be altered by Congress, by the courts, or by an administrative agency. We believe this is a momentous retreat from a concept that otherwise exists in multiple venues.<sup>9</sup> We agree that each of these venues for the expression of law does serve a purpose in shaping the contours of materiality, but we do not concede that they should be the exclusive venue. Indeed, FASB, which is comprised of accountants, might consider itself a body that could help identify the parameters of materiality.<sup>10</sup>

Defining materiality as a legal concept also makes a firm’s legal officer the pivotal arbiter of the issue. Currently an independent auditor might take a contest over whether an item should be discussed in the notes to the firm’s board audit committee. With this dynamic in force, the company’s financial officer might tend to accept the auditor’s recommendation instead of facing board arbitration. Under the new FASB rubric, a dispute between the auditor and in-house finance official will be settled by the in-house counsel. With this dynamic, the company’s auditor is less likely to contest the omission of what she might consider material information. In short, this dynamic will result in less information.

Even where the omission does, in fact, involve material information; it is not clear how a plaintiff will seek a remedy or how a court will weigh the evidence. If a company obtains a legal

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<sup>8</sup> In response to Public Citizen inquiry, FASB representatives pointed to three “stakeholders” that were not “issuers” or accountants. These are representatives from a. the Center for Financial Research and Analysis; b. Standard & Poors; and c. Lazard Freres. The first is a group that specializes in forensic accounting, a business model that profits from finding what’s not transparent. The other two cannot be considered independent consumers of financial information, as their clients are issuers. Email from FASB available upon request

<sup>9</sup> These venues include the law, facts, and markets, which can be influence by emotion. Information contained in print may have a different impact than video. For example, it may be immaterial that a CEO is arrested for DUI. However, if this arrest is captured on video, this may lead to a different impression of the same information. See discussion, available at: <http://www.theconglomerate.org/2010/10/is-your-ceo-being-arrested-for-dwidui-material.html>. In another case, a CEO was caught on a surveillance camera abusing his dog. This became public, and the company was forced to issue a statement condemning its CEO. See San Diego Union, available at: <http://www.sandiegouniontribune.com/news/2014/aug/25/centerplate-ceo-dog-kicking-san-diego-contracts/>

<sup>10</sup> DELETE OR REWRITE

opinion from its in-house counsel, a plaintiff may need to establish the legal incompetence of the in-house counsel. The issue of accounting competency will be irrelevant.

We urge FASB to withdraw its proposal. We ask that it reconstitute an advisory panel composed of financial information users. The concept of materiality is important, and we look forward to a good faith effort to better help issuers to inform their investors.

Sincerely,

Public Citizen,  
Pax World Management LLC  
Greenpeace  
New Progressive Alliance  
Harrington Investments, Inc  
CREDO  
International Brotherhood of Teamsters  
Center for Effective Government  
Global Witness  
US PIRG  
Michael Greenberger, Law School Professor, University of Maryland Carey School of Law  
Daily Kos