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2015-300
Comment Letter No. 12
2015-310
Comment Letter No. 20
330 North Wabash, Suite 3200
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December 5, 2015

Via email to director@fasb.org

Susan M. Cosper
Technical Director
Financial Accounting Standards Board
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Re: Notes to Financial Statements (Topic 235): Assessing Whether Disclosures Are Material (File Reference No. 2015-310) and Conceptual Framework for Financial Reporting: Chapter 3: Qualitative Characteristics of Useful Financial Information (File Reference No. 2015-300)

Dear Ms. Cosper:

We are pleased to provide comments on the Board's proposal to improve the effectiveness of disclosures in the notes to the financial statements. While we strongly support the objective, we are not optimistic the exposure drafts will result in that outcome for several reasons.

The proposal appears to expand the number of materiality assessments that may be required because some entities currently assess the materiality of disclosures related to a financial statement line item on an all-or-nothing basis. For example, if intangible assets are not material to the entity, then none of the associated disclosures are considered material. However, the proposal would require an assessment of potential disclosures "individually and in the aggregate." The rigor of each individual analysis would vary, but a robust consideration of the quantitative and qualitative factors outlined in SAB 99 with respect to each specific disclosure requirement in a Codification Topic seems impractical. Similarly, the proposal introduces a distinct assessment of materiality for footnote disclosures compared to amounts that are presented in the financial statements. If our understanding is correct, this would also increase operational burdens for preparers and auditors, while seemingly adding minimal value to users of the financial statements.

Separately, we struggle with the notion that materiality should be increasingly understood as a legal concept. Accountants have a tradition of assessing materiality for purposes of financial reporting. While legal considerations can be a relevant factor, we are concerned that the statement "Materiality is a legal concept" will encumber, rather than ease, the ability of accountants to exercise professional judgment, particularly if the effect of this language is to increase the need to regularly obtain legal counsel.¹

In light of these challenges, our preference would be for the Board to revisit existing disclosure requirements. This might include improving existing disclosures and/or eliminating those that are

¹ In this context, it is also unclear whether and how the SEC staff would revise SAB 99 to further address legal concepts since staff accounting bulletins reflect the SEC staff's views regarding *accounting-related* disclosure practices for registrants (see <http://www.sec.gov/interp/account.shtml>; *italics added*).

Technical Director
Financial Accounting Standards Board
Page 2 of 6

redundant or that no longer provide useful information to investors. Our premise is that diminishing returns set in, no matter how well-intentioned the most recent disclosure requirement is. In other words, we believe it is more efficient and effective for the standard-setter to set and eliminate disclosure requirements than it is for preparers and counsel to expand the frequency of materiality assessments for a growing list of disclosure requirements.

These points and others are included in our responses to the Board's specific questions in the Appendix to this letter. We would be pleased to discuss our comments with the FASB staff. Please direct questions to Adam Brown at (214) 665-0673 or Gautam Goswami at (312) 616-4631.

Very truly yours,

A handwritten signature in black ink that reads "BDO USA, LLP". The letters are cursive and slightly slanted.

BDO USA, LLP

Appendix

Question 1: Would assessing materiality subject to the proposed changes to paragraphs 235-10-50-7 through 50-8 be any easier than under current GAAP? If yes, please explain why.

We are not optimistic that assessing materiality will be easier under the proposed changes than it is under current GAAP. Our concern is based on several factors.

First, the proposal appears to expand the number of materiality assessments that may be required. Specifically, preparers may need to assess whether a financial statement line item is material (e.g., an investment in marketable securities) as well as each of the individual related disclosures (e.g., each of the items in ASC 320-10-50-1 through 50-14). For entities that currently assess the materiality of disclosures related to a financial statement line item on an all-or-nothing basis, the language proposed in paragraph 235-10-50-7 that requires an assessment of potential disclosures “individually and in the aggregate” will take additional time and effort. The rigor of each analysis would vary, but a robust consideration of the quantitative and qualitative factors outlined in SAB 99 with respect to each specific disclosure requirement in a Codification Topic and aggregation of such seems impractical.

Second, the proposal introduces a seemingly distinct assessment of materiality for disclosures compared to amounts that are recognized and measured in the financial statements. If our understanding is correct, this would also increase operational burdens for preparers and auditors because it creates a scenario where an asset or liability is material on the balance sheet, but disclosures related to that same element are not considered material or vice versa. Attempting to reconcile those disparate outcomes could be time-consuming and challenging.

Third, and perhaps most important, we struggle with the notion that materiality should be increasingly understood as a legal concept. Accountants have a long tradition of assessing materiality for purposes of financial reporting. While legal considerations can be a relevant factor, we are concerned that the statement “Materiality is a legal concept” will encumber, rather than ease, the ability of accountants to exercise professional judgment. This is particularly true if the effect of this language is to increase the need to obtain input from attorneys on a regular basis. If attorneys are to be consulted for numerous individual disclosures at each interim and annual period, this will necessarily make the financial reporting process lengthier. Further, it is unclear whether attorneys would be able to provide unqualified legal advice as to whether a particular disclosure is material or not. In current practice, formal legal advice is typically accompanied by numerous assumptions and caveats. As such, the proposal may not result in any significant improvement as entities may err on the side of caution, with the unintended consequence of continued “boiler-plate” disclosures.

In light of these challenges, our preference would be for the Board to revisit existing disclosure requirements. This might include improving existing disclosures and/or eliminating those that are redundant or that no longer provide useful information to investors. Our premise is that diminishing returns set in, no matter how well-intentioned the most recent disclosure requirement is. Therefore, reconsidering and eliminating (where possible) individual disclosures will enhance the ability of investors to focus on information that is most important without significantly increasing the cost to preparers, which is otherwise a likely outcome if this proposal is adopted. We believe this is a more direct manner of improving the effectiveness of the present disclosure regime, while also providing relief to preparers. In other words, we believe it is more efficient and effective for the standard-setter to set and eliminate disclosure requirements than it is for

Technical Director
Financial Accounting Standards Board
Page 4 of 6

preparers and counsel to expand the frequency of materiality assessments for a growing list of disclosure requirements.

Question 2: Would applying the amendments in this proposed Update significantly increase or reduce costs of preparing the notes to financial statements? Why or why not?

Please see our response to Question 1.

Question 3: Would the amendments in this proposed Update change the information you otherwise would include in the notes to financial statements? Why or why not? If yes, how would that increase, diminish, or otherwise change the notes' usefulness to investors, creditors, and other financial statement users?

We do not expect the amendments to significantly change the information currently provided in the notes to the financial statements. Currently, if preparers decide not to disclose an item required by GAAP, it leads to discussions with the auditors and the company's audit committee regarding this so-called "error" (assuming it is more than trivial). By stating the omission of an immaterial disclosure is not considered an error in paragraph 235-10-50-9, we believe the thrust of that conversation will shift to a discussion of materiality. As such, an incentive will still exist for preparers to comply with the disclosure requirement rather than preparing and discussing a potentially time consuming materiality assessment with the auditors and the audit committee.

Question 4: Do you expect regulatory, legal, or audit consequences that would affect your ability to consider materiality when selecting information to be disclosed in notes to financial statements? Please explain.

It is possible the proposal could add to existing tensions with certain regulatory bodies and the entities they oversee. For example, we understand insurance and banking regulators focus on particular footnote disclosures that are relevant to their public policy objectives (e.g., prudential oversight) such as related party activity, regulatory capital ratios, and fair value information. Similarly, there are transactions that must be reported to the IRS under current U.S. federal tax law even when the expected tax effects might not be material for purposes of U.S. GAAP. As a result, it is unclear how preparers would consider these factors when assessing the materiality of various footnote disclosures from a legal standpoint.

Also, an increased emphasis on the legal concept of materiality may result in additional resource constraints and increased costs with arguable benefits for companies that do not currently employ such legal expertise in-house.

Moreover, there are currently incentives in the financial reporting system that can conflict with each other despite existing language in the Codification which states its provisions do not need to be applied to immaterial items.² To illustrate, a company may comply with a disclosure requirement to mitigate legal or regulatory risk, while at the same time limiting that disclosure to "the letter of the law" in order to avoid perceived competitive harm. It does not appear the exposure draft would significantly alter that dynamic.

Question 5: How would you disclose information in comparative financial statements if your assessments of materiality differed in different years?

² 105-10-05-6

Technical Director
Financial Accounting Standards Board
Page 5 of 6

This question appears to imply preparers should continually revisit prior period disclosures based on current materiality assessments. We do not believe any clear incentive exists to justify this practice. A requirement to that effect would appear to create incremental cost without clear benefits. Specifically, many investors look to the disclosures provided in the current period for the most relevant information. We do not think companies or their investors would find more value in assessing and updating prior period disclosures. As such, we believe the results of a materiality assessment should inform current period disclosures without calling into question prior disclosures.

Question 6: Should the Board eliminate from the Accounting Standards Codification phrases like “an entity shall at a minimum provide” and other wording that could appear to limit an entity’s discretion to omit immaterial disclosures? Are there particular Topics or Sections in which those changes should not be made? Are there additional paragraphs within the Accounting Standards Codification in which the wording is particularly restrictive and is not identified in Appendix B of this proposed Update? If so, please identify them.

Since entities are generally not prohibited from making voluntary disclosures, we would not object to removing phrases like “an entity shall at a minimum provide” certain prescriptive disclosures. As indicated in our response to Question 1, we believe revisiting existing disclosure requirements and identifying those that are redundant or no longer useful would achieve the same purpose in a more effective and efficient manner.

Question 7: Do you agree with the proposed amendment that would explicitly state that the omission of an immaterial required disclosure is not an accounting error? Why or why not?

We are sympathetic to this language and the relief it is intended to provide by emphasizing the existing requirement that accounting guidance need not be applied to immaterial items. However, it is unclear why this emphasis is considered necessary only for disclosures and not for recognition and measurement.

Question 8: Are there considerations other than those discussed in this proposed Update that would apply to not-for-profit entities?

With respect to the basic concept of materiality and providing relevant disclosures to inform users of the financial statements, we believe the considerations in the proposed ASU are generally the same for not-for-profit entities.

Question 9: Should the proposed amendments be effective upon issuance?

We recommend allowing at least one year or more for adoption if a final standard is issued. As indicated above, it is possible a final ASU as proposed may create unintended consequences, including potential interactions with the audit standards and the law that may come to light as entities prepare for implementation, including having to update disclosure checklists focusing on a legal concept. A reasonable adoption period would be consistent with other ASUs, particularly in light of several other major standards that will take effect in the near future, which will introduce new disclosure requirements of their own (revenue, leases, financial instruments, etc.).

Technical Director
Financial Accounting Standards Board
Page 6 of 6

**Part II: Conceptual Framework for Financial Reporting: Chapter 3: Qualitative Characteristics
of Useful Financial Information**

Question: Do the proposed amendments improve Concepts Statement 8? If so, how? If not, why?

Similar to our thoughts on the proposed ASU for Topic 235, we question whether a more explicit shift to a legal understanding of materiality will be an improvement. We believe this may cause entities to incur more time and expense to assess materiality, as well as the frequency of those assessments.

In addition, relying on the law implies entities would need to deepen their understanding of the legal environment, particularly for multi-national entities. To the extent a reporting entity conducts operations in different countries, it is unclear how competing legal doctrines across jurisdictions would be resolved. This situation would also be compounded by the fact that the laws of a given jurisdiction change over time.

In this context, we do not currently see sufficient benefits to supersede the existing definition of materiality in Concepts Statement 8.