November 13, 2020

Via email to director@fasb.org

Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Comments on Proposed Statement of Financial Accounting Concepts No.8, Conceptual Framework for Financial Reporting (Ch. 4: Elements of Financial Statements)

Dear Technical Director,

As Case Western Reserve University master of accountancy students at the Weatherhead School of Management, we appreciate the opportunity to comment on the **proposed Statement of Financial Accounting Concepts No.8, Conceptual Framework for Financial Reporting (Ch. 4: Elements of Financial Statements)**.

We support the Board's attempt to improve the already solid framework by identifying elements of financial statements that could be appropriate for recognition in the financial statements and relevant to the users of those financial statements. The proposed chapter seeks to provide the Board a framework for developing standards that enhance 'interested parties' understanding of the reporting entity.

Our detailed comments are included in the attached Appendix. If you have any questions regarding the comments, please contact Noah Mehrle, 513-293-1374 or Colden Schemmel, 440-222-6110.

Sincerely,

Summary:

After reviewing the proposed Statement of Financial Accounting Concepts No.8, Conceptual Framework for Financial Reporting (Ch. 4: Elements of Financial Statements) and answering the questions for respondents, we found that we agree with the majority of the Board's proposals. In particular, the definition of an asset and the definition and presentation of revenues versus expenses are to our liking. However, we request further clarity regarding the definition of certain liability elements. Firstly, we thought certain circumstances surrounding the specifics of repayment regarding certain liabilities were not adequately addressed. Secondly, we were unclear as to the implications surrounding certain obligations being legally binding.

Appendix: Questions for Respondents

Question 1: The Board expects that most assets that met the definition of an asset in FASB Concepts Statement No. 6, Elements of Financial Statements, will continue to qualify as assets under the definition of an asset in this proposed chapter. Do you agree that the definition of an asset in this proposed chapter is consistent with the Board's assertion? If not, please provide examples.

We agree with the Board's definition of an asset. Specifically, that this element is a present right to a potential future economic benefit. Therefore, we also agree that the vast majority of, "assets", as defined in FASB Concepts Statement No. 6, Elements of Financial Statements, remain correctly classified as such. Oftentimes it is made easier to identify assets because they are; contractual, tangible, exchangeable, and/or separable. However, it is not absolutely necessary that this is the case.

Question 2: In particular, respondents are asked to focus on internally generated intangible assets. Is the definition of an asset in this proposed chapter helpful in resolving issues of identifying intangible assets?

We agree that the definition of an asset, as proposed in this chapter, is helpful in identifying and resolving issues surrounding intangible assets. Whether or not the asset takes on a physical form does not have any bearing on an entity's right to that asset or the potential for future economic benefit attached to that asset. According to Paragraph 36 of the chapter four proposal, if the entity is capable of exchanging or separating the intangible asset for something of value, there is evidence that a right exists. This is regardless of whether or not a contractual relationship has been established. This goes hand in hand with the potential future economic benefit. Thus, internally generated intangible assets fit squarely within this chapter's definition of an asset.

Question 3: The Board's definition of an asset in this proposed chapter does not include the term control. However, this proposed chapter explains why and how control is interrelated to the definition of an asset. Is this discussion sufficient or is the term control necessary to include in the definition of an asset? If the term control is necessary to include, please explain how its inclusion would change the population of items that would meet the definition of an asset in this proposed chapter.

We agree with the board's decision to eliminate the term, "control" from the definition of an asset. This term was misleading as it implied that in order for a trade receivable, for example, to be considered an asset the receiving entity must have had decision power over that benefit. Yes, the entity has the right to hold the receivable or sell it to a third party, however in the end the receivable may not be collected in full or at all. Instead, "present right", as outlined in BC4.17, does a much better job of driving home the concept that the ability to deny or regulate access to that benefit is what constitutes the right to an asset. That being said, the concept of control is generally helpful in understanding what constitutes an asset. Therefore, we agree with the term's description being included.

Question 4: The Board decided that an obligation to transfer either assets or, in certain limited circumstances, an entity's own shares would meet the definition of a liability. Is the discussion in this proposed chapter of the limited circumstances in which the entity's own shares would meet the definition of a liability sufficiently clear?

We do not believe that the proposed chapter's discussion surrounding the use of an entity's own shares meeting the definition of a liability is sufficient. The proposed chapter, in our opinion, should have included specifics surrounding how the value of the liability will be upheld even as the stock price fluctuates. It should be made clear that if a liability is owed and stock is used to pay, the entire amount must be paid regardless of the share price. Additional shares will simply be added to the consideration if their individual prices decline.

Question 5: Other than as described in Question 4, to allow certain share-settled instruments to be liabilities, the Board expects the liabilities that met the definition of a liability in Concepts Statement 6 will continue to qualify as liabilities under the definition of a liability in this proposed chapter. Do you agree that the definition of a liability in this proposed chapter is consistent with the Board's assertion? If not, please provide examples.

We agree with the amendments, made by the board in Proposed Chapter 4, to the definition of a liability. In BC4.10, they did away with the term, "probable" because it was often misinterpreted to mean that a liability only ought to be recognized when it was probable to have to be paid in the future. For instance, potential lawsuits constitute a contingent liability for many entities in the United States. It is difficult to quantify the percentage chance of being ordered to pay this form of liability. Also, it can be difficult to quantify the dollar amount associated with that potential loss. For this reason, we agreed with the “probable” threshold being eliminated.

We also agree with the decision to eliminate the term “future” from the definition of liability. Doing so clears up the confusion regarding present obligation versus future obligation. If you have entered into an obligation with another entity, it is important to understand the current nature of that debt. You owe potential economic benefit even though it has not yet technically become due. Also, entities have the option to pay off debt early. This would save them money in the form of interest and would result in no future obligation regardless of the initial terms of the agreement. For these reasons, we agree with removing this term.

Thirdly, the proposal eliminated the terminology “ past transaction”. This is a minor but positive change. The board concluded that if we are discussing events that generated a present obligation, then one can deduce that these events occurred in the past. For this reason, we like the change.

Finally, in E49, the proposed change seeks to clarify when an entity becomes presently obligated. This occurs when the obligation is legally enforceable. This situation often arises from binding contracts, agreements, rules, or status that mandate certain behavior on behalf of the entity.

Question 6: In practice, the more challenging applications of the definition of a liability in Concepts Statement 6 were related to business risks, constructive obligations, and stand-ready obligations. Is the discussion of those three areas in this proposed chapter adequate to understand and apply the definition of a liability?

Elements 47 & 48 of Concepts Statement 6 specifically address business risks and their application to the definition of a liability. In our opinion, the contents of both Elements, which describe business risks, are sufficient enough to understand and adequately apply the definition of a liability. These respective passages make clear that just because there is a presented risk, this does not create a present obligation which is one of the essential characteristics of a liability. The examples pertaining to the ‘airline company’ and ‘skilled workers’ help further explain these concepts.

In the following passages, Elements 50-54, the statement addresses constructive obligations and their application to liabilities. It is in our opinion that this section creates confusion surrounding the nature of constructive obligations. The contents of these passages address that oftentimes constructive obligations create a present obligation but are not legally binding. In other words, instead of an obligation being created by a contractual agreement, one is created by the facts. With that in consideration, we remain unclear about the implications of a constructive obligation having no legal sanction, versus a legally binding liability.

Lastly, we feel the sections, Elements 59-63, are sufficient in covering the nature and application of stand-ready obligations to the definition of a liability. Most importantly, we like how Concepts Statement 6 made the distinction between a stand-ready obligation and a business risk. Where the former creates a present obligation with an uncertain amount, the latter creates no present obligation despite likelihood of occurring.

Question 7: The Board suggested that integration with presentation principles would be helpful in distinguishing between the components of comprehensive income. To facilitate this distinction, paragraph E92 of this proposed chapter references presentation principles. Is distinguishing revenues from gains and expenses from losses essential as a matter of elements, or should those distinctions be exclusively a matter for presentation concepts? Please explain.

We believe that distinguishing revenues from gains and expenses from losses should be essential as a matter of elements rather than a matter for presentation concepts. However, when revenues and gains and expenses and losses are difficult to distinguish from one another, we agree with the Board's determination that presentation concepts may be more applicable. It appears from the Chapter that the Board will continue allowing this twofold approach. The probability of items being difficult to distinguish is inherently low. In those cases, we feel presentation concepts enhance financial reporting rather than guessing whether an item is a revenue or gain, or an expense or loss. Therefore, we feel that items will be fairly presented using this approach along with adequate disclosure.

Question 8: As described in Question 7, this proposed chapter seeks to distinguish between revenues, expenses, gains, and losses. Do the definitions of and other explanatory language related to revenues, expenses, gains, and losses make the distinction between these elements sufficiently clear?

We do indeed believe that the definitions discussed in this proposed chapter related to revenues, expenses, gains, and losses are sufficiently clear and distinct from one another. For example, we find it clear that revenues stem from inflows of assets or settlements of liabilities; while gains come from increases in other events, transactions, and circumstances. We feel that these definitions are sufficient enough to distinguish between revenues and gains most of the time. Likewise, we feel the same way in regard to expenses and losses. Given the difficult nature behind formulating these definitions, we feel the Board was succinct and effective in formulating the explanatory language.

Question 11: "Appendix A: Accrual Accounting and Related Concepts," includes discussion of several concepts that are used in this proposed chapter and in other chapters of the Conceptual Framework. Is this material helpful in a chapter discussing the elements of financial statements?

Yes, we believe that discussing accrual accounting and related concepts is helpful alongside elements of financial statements. We acknowledge that it is a bit of a departure from defining elements of accounting and giving real-life examples. But, nevertheless, we see the merit in discussing the preeminent accounting method to be used in conjunction with said elements. With few exceptions, all publicly traded companies are required to use accrual accounting. So, it's an absolute must for accountants to have a deep understanding of accrual accounting especially when intricate accounts that we've mentioned above like contingent liabilities are involved. For this reason, it is a wise decision on behalf of the board to include "Appendix A: Accrual Accounting and Related Concepts".