

FASB
401 Merritt 7
Box 5116, Norwalk, CT. 06856

To: The Technical Director

Regarding : Ref. 2015-310 on Materiality
Notes to Financial Statements (Topic 235)
Assessing Whether Or Not The Disclosures Are Material

From: Dr Joseph S. Maresca CPA,CISA

Colleagues,
Here are the member comments on Ref. 2015-310 -Materiality Notes to the F/S.
Details follow:

Background

The judicial application of the definition of materiality can be summarized by stating that disclosures generally should be evaluated as material based on whether or not there is a substantial likelihood that the omitted or misstated disclosure would have been viewed by a reasonable resource provider as having significantly altered the total mix of information available in making a decision.

Even though a misstatement of an individual amount may not cause the financial statements taken as a whole to be materially misstated, it may nonetheless, when aggregated with other misstatements, render the financial statements taken as a whole to be materially misleading.

In arriving at the decisions in this proposed Update, the Board received feedback that the Accounting Standards Codification could include the guidance that the Board's role is to broadly consider relevance, not materiality; that an entity is responsible for assessing materiality; and that the Board does not define or interpret materiality.

Existing phrases like "an entity shall at a minimum provide, which make it difficult to justify omitting immaterial disclosures, would be replaced with less prescriptive language.

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below.

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.

Answer:

The judicial application of the definition of materiality is more descriptive

because disclosures generally should be evaluated as material based on whether or not there is a substantial likelihood that the omitted or misstated disclosure would have been viewed by a reasonable resource provider as having significantly altered the total mix of information available in making a decision.

Omitted material can significantly alter the total mix of information available in very specific instances. For instance, suppose a customer International DDA account had a significant overdraft yet there were other accounts when netted on a consolidated basis produced overall good funds.

An auditor might overlook the overdraft; however, this lack of good funds in one account has implications for treating the overdraft as a loan with a specific rate of interest governed by contract in the overall relationship. And so, omitting the individual overdraft actually camouflages the theoretical waiver of overdraft interest by not disclosing the individual overdraft.

In addition, immaterial overdrafts in individual accounts could be material when combining groups of overdrafts in related accounts. The netting of overdraft accounts with good fund accounts in consolidation might mask fundamental weaknesses or suboptimality in the management of the customer's business.

The disclosure omission could mask fraud too. In practice, relationship officials must look very closely at the individual components of a customer relationship on a consolidated DDA basis.

The valuation of securities is another area subject to high volatility as evidenced by the VIX index. VIX is one popular measure of the market's expectation of stock market volatility over the next month.

High volatility as demonstrated by the VIX index will mean that valuations in individual portfolios are subject to wide swings up or down-sometimes due to purely irrational reasons. A related problem is that collateralized loans will have unstable security valuations due to unforeseeable investor fears and perceptions.

For the accountant, the practical problem involves reacting to and assessing sudden and sometimes steep market drops which impact collateralized loans, as well as, securities valuations themselves. In reality, market swings do alter the total mix of information available to decision makers, regulators and investors alike.

Foreign currency valuations is another area which impacts portfolios, loans made, receivables and other accounts. For instance, the ruble has varied widely. The ruble averaged 26.06 from 1993 until 2015, reaching an all time high of 72.45 in December of 2014 and a record low of 0.98 in August of 1993. (Retrieved from <http://www.tradingeconomics.com/russia/currency>)

The implications for accountants is in the area of settling loans when a debtor currency (i.e. Russia) drops precipitously. When a debtor's currency drops, (in this case Russia) more rubles must be paid to purchase a single dollar in order to pay down the debt.

The other way to alleviate the burden is for the creditor's currency to devalue so that fewer rubles are needed in conversion to acquire dollars to pay off the debt.

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?

Much depends upon such things as volatility as explained above. If markets are stable, transaction handling is more predictable. If markets are unstable, account balances in some cases are more difficult to determine with any level of consistency and data comparability. The instability will result in increased costs and delayed financial reporting because judgments may be made difficult due to unknown or unquantifiable factors. The notes to financial statements may be more voluminous because assumptions may have to be made and explained more fully.

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?

Information could change based upon relevance, as well as, the likelihood of errors due to market uncertainties or the conditional probabilities of events like currency devaluations, significant stock market swings, expropriations and random events which could alter disclosure requirements.

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.

Materiality is more difficult to determine in an uncertain market environment. In some cases, a linear regression line can be drawn as a predictor based upon a long string of historical data.

Question 5:

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

If the assessments of materiality differed substantially, statements might have to be restated in individual cases based upon the needs of the strategic constituencies like the Securities Exchange Commission or the National Association of Securities Dealers (NASD).

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?

An alternative might be that an entity provide a reasonable disclosure to minimize errors and mis-statements within a relevant range that satisfies the good judgment exercised by the accountant in the circumstances.

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?

Probably not. The reasoning is that immaterial balances can evolve into material ones-especially during periods of market instability.

Question 8:

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

Not-for-profit entities are judged by program effectiveness and quantifiable benefits to the public arising from the non-profit operations.

Question 9:

Should the proposed amendments be effective upon issuance?

Much depends upon the timing requirements recommended referred to in the member comments.

Sincerely,
Dr Joseph S. Maresca CPA, CISA