



Financial Statement Disclosure – How Much is Just Right?

by Eliza Ong

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Financial statements are an invaluable communication tool to investors.

However, preparers are burdened with the time and cost of preparing increasingly more disclosures, while users have to sift through pages of footnotes to obtain useful information.

In this article, Eliza Ong of Mind the GAAP asks “how much disclosure is just right”?



Background

Both the FASB and IASB are working on ways to address “disclosure overload”.

- In July 2012, the FASB issued a Discussion Paper outlining a potential new framework that would help inform the Board when disclosure might be necessary and appropriate.
- In January 2013, the IASB hosted a public forum to discuss the causes of disclosure overload and ways to resolve this issue. Attendees included preparers, users, regulators, standard setters, and auditors. Following this forum, the IASB subsequently published a Feedback Statement, in which the IASB committed to perform further research on the concepts of materiality and disclosure effectiveness. The IASB is also considering amendments to IAS 1 including potentially defining, and requiring presentation, of EBITA.

What is the disclosure problem?

The IASB carried out a survey in December 2012 to get a better understanding of the disclosure problem in advance of the discussion forum.

Over 80% of the 233 respondents believed that too much irrelevant information was being presented in the financial statements, suggesting that companies were presenting immaterial information because they were required to do so by IFRS, regulators, or their auditors.

Interestingly, users didn’t necessarily agree that too much information was being presented, but instead felt that companies did a poor job of communicating or highlighting the most important disclosures.

Also, financial statement users, in particular, complained that companies often used generic language and did not customize disclosure for the specific facts attributable to a given reporting entity.

Making the complex understandable



What is the root cause?

Many respondents to the IASB survey, as well as attendees at the IASB's forum believe that companies, regulators and auditors currently use a "checklist mentality" towards financial reporting. As a result, constituents feel the need to include discussion around each and every disclosure mentioned in IFRS or U.S. GAAP, resulting in a lot of immaterial information being reported in a boilerplate (i.e., non-entity-specific) manner.

Users also noted that a checklist mentality results in preparers being less willing to disclose potentially useful information that technically is not a requirement of U.S. or international accounting rules.

How much disclosure is just right?

To solve this problem, it seems like we should revisit a fundamental question – namely, what is the purpose of the financial statements? Per the IASB Conceptual Framework, financial reporting provides information for the investors and creditors to make decisions about:

- Their investment or debt and
- How effectively and efficiently management has discharged their responsibilities to use the entity's existing resources (i.e., stewardship).

To meet the goals of financial reporting, Mind the GAAP believes that disclosures should be based on **material, entity-specific information**, rather than simply ticking off a boilerplate checklist. This would involve a significant change from a compliance mindset on the part of preparers, auditors and regulators to one that involves the exercise of greater professional judgment.

We believe that a robust principles-based disclosure framework that has a proper balance between specific disclosure requirements and preparer flexibility will help achieve this objective. The benefits of a flexible approach – particularly, allowing companies to focus on areas that are most meaningful and relevant for their circumstances – outweigh the costs, such as the potential for a lack of disclosure consistency between comparable companies.¹

For more detailed information regarding our views, please refer to our [2012 comment letter](#) or contact a representative of Mind the GAAP at +1 773.732.0654 or info@mindthegaap.com.

¹ Over time, we suspect market forces and regulatory reviews will mitigate this potential concern anyway.