

3. Overview of Professional Accountant's Perspective

This section provides an overview of important information related to the perspective of an accounting manager or member of a team creating a financial report, an internal auditor or third party auditor evaluating such a report, a CFO signing off on such a report, or an audit committee evaluating the information expressed within a financial report. This information is not a comprehensive summary of all considerations; rather it is a brief overview of considerations which would generally not be disputed.

HINT: It is very important to recognize that the historical mediums used to express financial information such as paper and electronic forms of paper such as HTML or PDF are structured for presentation of information and therefore only understandable by humans. They were not structured to represent the meaning of the information. Digital mediums such as XBRL are structured to represent meaning and are therefore readable by machines such as computers. The meaning can also be used to present the information as desired. Understanding these differences helps professional accountants understand how to best employ these new mediums.

3.1. *Financial reports tell a story*

A financial report tells a story. The story which is communicated by a financial report does not change based on the medium used to tell that story. The meaning of the financial information articulated by the creator of the financial report and the meaning of the financial information derived by the users of the financial report should be the same. Both the creator and consumer should walk away with the same message or story. Creators of a financial report go to great lengths to tell the story which they believe best reflects the financial condition and financial position of the reporting economic entity providing the financial report.

Creators and users of a financial report are free to interpret the information communicated by the message/story of that financial report as they see fit. But, the information itself should be identical for both the creator and user. Reported information is facts. For example, if a fact is reported and the fact is deemed to relate to the consolidated entity, be as of December 31, 2014, for the US GAAP concept "Cash and cash equivalents", being expressed in US dollars; then the derived meaning and understanding should not be in dispute between two different parties who are using the same piece of financial information. However, any party is free to interpret the facts as they deem appropriate.

3.2. *Separating facts from opinions*

Senator Daniel Patrick Moynihan said: "Every man is entitled to his own opinion, but not to his own facts." Both **facts** and **opinions** exist within financial reports.

There are at least three separate questions which must be answered by an accountant creating a disclosure for, or presenting information within a financial report. Understanding these three questions and separating them in one's mind helps one express the financial information using digital medium appropriately.



The first question is, "Which disclosure(s) are appropriate?" This question requires professional judgment and can only be correctly answered by a qualified, trained professional accountant. The answer to the question tends to be part fact and part opinion. The second question, "How is the information best placed, shown and/or formatted within the financial report?" The answer to this question tends to be more based on arbitrary personal preference and therefore is more subjective than based on fact. The third question, "Given a certain disclosure, what is the information being disclosed and how does it relate to other information?" The answer to this question tends to be more objective than subjective and is governed by rules of logic and mathematics.

In fact, the financial reporting conceptual framework explicitly tries to make financial report disclosure as objective as possible. You can see this in the goals articulated for the conceptual framework (per the FASB Special Report, *The Framework of Financial Accounting Concepts and Standards* (1998):

- Providing a set of common premises as a basis for discussion
- Provide precise terminology
- Helping to ask the right questions
- Limiting areas of judgment and discretion and excluding from consideration potential solutions that are in conflict with it
- Imposing intellectual discipline on what traditionally has been a subjective and ad hoc reasoning process

To put these questions in more concrete terms we will use an example. Say a reporting entity must release a financial report. The accountant can pick between options such as providing a balance sheet or a statement of net assets. Industry practice, common practice, and rules and regulations all come into play with this choice between available options. Further, the accountant knows that he or she is required to provide a cash flow statement; but that accountant can pick between using the direct method or the indirect method to create that cash flow statement, that is subjective.

But if a balance sheet is chosen by the accountant, then assets must be provided, liabilities and equity must be provided, and assets must equal liabilities and equity on that balance sheet. The model of the balance sheet is known and an accountant has no latitude and gets no voice in saying what a balance sheet is; regulators and standards setters dictate those rules. Accountants and the financial information which exists can determine many of the line items which are appropriate for the balance sheet. These mechanics of a balance sheet are well understood by accountants, although they may not necessarily think of balance sheets in this way.

Other items are purely objective. For example, the accountant can choose to format zeros by showing a blank, showing a "0" or showing "-"; but the meaning is always the same, zero.

Understanding the distinction between what is a fact and what is an opinion helps accountants understand things that they can decide and where they simply need to follow the rules.

A *fact* is a statement that can be proven to be true or false using logic or evidence. A fact is something that exists and is objective. An *opinion* is a statement or expression of a person's feelings. Opinions indicate a belief. Opinions cannot really be proven, only expressed. Opinions are subjective. Opinions can be based on facts, preferences, beliefs, interpretations, emotions, and even desired outcomes.



Opinions can be meant to deliberately mislead others. Including certain facts, excluding certain facts, or misrepresenting facts are tactics for expressing an opinion.

Sometimes there may be a fuzzy line between a fact and an opinion. Sometimes there are fuzzy lines between allowed accounting rule alternatives and ambiguity in the financial reporting standards. Allowed alternatives and unintended ambiguity are not the same thing.

How digital mediums work, such as the XBRL medium, is based on facts, and indeed must be based on only the facts. XBRL is a global technical specification, an agreement on how XBRL works, technical specifications are objective.

3.3. Facts are more important than organization or formatting

What is more important to report, the facts themselves including the “packaging” such as formatting, or just the facts?

For example, a Journal of Accountancy article *FASB sees flexibility, relevance as cures to disclosure overload*²⁵ states that the FASB is asking for feedback on whether ordering and formatting should be:

- Flexible and based on relationships of particular items;
- Flexible and based on the importance of particular disclosures; or
- Fixed and uniform.

With technologies such as XBRL which allow financial information to be expressed digitally is there really a need to make a choice? All three options are possible at the same time. Is this list of options a remnant of the way of thinking constrained by old paradigms which are no longer applicable in a digital world? Why can't the user of financial information have all three options available and the user can pick which reported facts are appropriate for their use of the information and which approach is best for them given their preferences and their perceived needs?

3.4. True and fair representation of financial information

Clearly the financial information provided by a reporting entity should not be “untrue” or “unfair”. As such, by definition it should be “true” and “fair”. Based on the rules, regulations, and common practices which exist; based on the informed professional judgment of the accounting team expressing the financial information; and considering all the other factors which must be considered when a reporting entity expresses its financial information, tells its story; that story should obviously be a true and fair representation of such financial information.

The story itself and the medium used to tell the story are two different pieces of the same puzzle.

Accounting teams are responsible for creating and verifying for themselves that they have created a true and fair representation of their financial information, regardless of which medium is used to express that information. And, regardless of which medium is used, that information must be: complete, correct, consistent, accurate. Each reported fact must have fidelity, which is to be a faithful representation. The set of all facts must fit together appropriately, the integrity must be sound.

²⁵ *FASB sees flexibility, relevance as cures to disclosure overload*, <http://www.journalofaccountancy.com/news/2012/sep/20126364.html>



Considered holistically from all points of view, the multiple pieces of the system work together correctly, all things considered. If this is true and a report possesses these characteristics, and if it is true and fair, it is then considered to be a “valid” or desired result. The financial report can be considered a desired result, free from logical flaws, based on sound reasoning, in other words cogent.

Verification is the process of asserting truths and understanding for oneself that information is valid per those assertions. Verification can be internal, external, and/or independent third-party verification. Verification can be performed by humans manually, or verification can be performed by computers using automated processes. Automated verification tends to be cheaper and more reliable than human verification.

3.5. Quantitative and qualitative; objective and subjective

Reporting entities have flexibility to provide/present disclosures differently as long as all the required disclosures are met and other compliance rules are complied with. The primary financial statements and notes to the financial statements are an organization or presentation of required disclosures.

Accountants creating financial reports use both **quantitative measures** and **qualitative measures** to provide such disclosures.

“*Quantitative measures*” means that you use an actual number to disclose an amount or to show a change. For example, “net income for the year was \$1,000,000” is a quantitative measure.

“*Qualitative measures*” means not showing an actual number, but rather providing information in other ways such as using relative terms. For example, disclosing an entity’s objective for holding or issuing derivative instruments, background information necessary for understanding those instruments, strategies used to meet those objectives, and information helpful in understanding derivative activity is a qualitative measure.

Some disclosures tend to be rather **objective** in nature requiring little professional judgment. Other disclosures can be quite **subjective**, calling on a professional accountant to use their experience and judgment to provide the appropriate useful information.

“*Objective*” means that judgment is based on the facts of the situation and are not based on or influenced by personal feelings, preferences, tastes, or opinions. For example, the fact that balance sheets are included in financial reports and assets are part of a balance sheet is objective and there is no room for judgment.

“*Subjective*” means that judgment can be based on or influenced by personal feelings, preferences, tastes, or opinions. For example, whether a certain subsequent event is material and how to best disclose that event can be subjective, requiring significant professional judgment.

The overarching guidance to disclosing information is whether that information is **useful** in making decisions. To be useful, the information possesses the following characteristics: **relevance**, **reliability**, **comparability**, and **consistency**.

“*Relevance*” means that the financial information makes a difference when making a decision. The information matters.

“*Reliability*” means that the financial information is free from bias and errors.



“Comparability” means that a standard set of financial reporting principles are used. But given options, reporting entities are free to choose between allowed alternatives. For example, one company might use FIFO for valuing inventories and another uses LIFO.

“Consistency” means that a reporting entity uses the same standard accounting principle and reporting approach/method from period to period. For example, a reporting entity cannot flip-flop between FIFO and LIFO.

A few specific aspects relating to comparability and consistency are worth pointing out because they are often confused. Users of financial information often expect that every aspect of every reporting entity’s financial report be comparable to every other reporting entity’s financial reports. This is simply not the case. Financial reports are not, and should not, be a 'form' which is filled in by an accountant. One strength of US GAAP is its ability to let reporting entities report useful information specific to that entity.

Financial information reported by entities in the same industry sector tends to be more comparable than financial information reported by entities in different industry sectors.

A reporting entity's disclosures from period to period tend to be very comparable. While what disclosure information is considered useful by a given reporting entity for a given event, transaction, or other circumstance; once the disclosure approach is selected then the company specific disclosure of that information from period to period tends to be very consistent and comparable for any given reporting entity.

Accountants creating a financial report use disclosure rules/requirements, guiding principles, and their judgment when weaving together an appropriate financial report.

Some financial report disclosures tend to take the shape of very specific and objective quantitative measures. For example, the disclosure of earnings per share is an example of such a specific quantitative measure. These sorts of disclosures are like an "on/off" switch; either the disclosure is required or it is not and if it is required, what must be presented or disclosed is crystal clear. There may be judgment involved in computing or measuring the amount disclosed, but the need for the disclosure itself tends to be objective.

Other disclosures take the shape of being more subjective in nature and use more qualitative measures. For example in the derivative instruments example used above, the meaning of a business acquisition or divestiture to the overall financial position of a reporting entity and/or which information about the acquisition or divestiture is the important information depends on many different criteria and it is the role of professional accountants to exercise their judgment and determine the appropriate disclosures, all things considered, using known guiding principles.

Understanding which disclosures tend to take which shape and otherwise understanding these moving pieces is critical for financial report taxonomy creation, financial report creation, and analysis of financial information expressed by these taxonomies and financial reports.

There are times when a certain specific financial disclosure in two different financial reports will be very different, each reporting different facts. Both financial disclosures being appropriate for the circumstances and both satisfy prescribed disclosure rules/requirements, both being useful, etc.



Other times facts disclosed should be identical for reporting entities.

3.6. *Identifiable, definitive, discrete set of pieces*

The information contained within any financial report is an identifiable, definitive, discrete set of reported facts. Those facts have an identifiable, definitive, discrete set of characteristics. Those facts and characteristics have an identifiable, definitive, discrete set of relations between other facts. Those facts and characteristics have an identifiable, definitive, discrete set of properties. These facts, characteristics, properties, and their relations must be clear, consistent, logically coherent, and unambiguous (as opposed to vague, inconsistent, incoherent, and ambiguous).

While determining what must be reported and how it is reported can at times be subjective in nature and require significant professional judgment; once that judgment has been exercised and once the information is provided the facts, characteristics, relations, and properties of that reported information is in no way subjective and open to judgment.

All facts, characteristics, relations, and properties can be identified; they are physical objects which can be observed. As such, they are objective. The mechanics of the objects which comprise a financial report are not a mystery; rather, they tend to be well understood.

Below is a summary of the risks which could lead to a financial report being invalid and the risk mitigation assertion or verification task which would assure that the risk goes unrealized. Terminology of the *Financial Report Semantics and Dynamics Theory*²⁶ is used to clearly state the report objects, relations, and properties which must be examined either using automated processes or manual processes to verify that object property. The risk and mitigation is independent of whether the verification task is performed by a party which is or is not independent.

Risk	Risk Mitigation Assertion (Verification task)
Full inclusion: All relevant facts, characteristics which describe facts, parenthetical explanations of facts, and relations between facts/characteristics are not included in the financial report.	Completeness: All relevant facts, characteristics of facts, parenthetical explanations of facts, and relations between facts/characteristics have been included.
False inclusion: No facts, characteristics which describe facts, parenthetical explanations of facts, or relations between facts/characteristics which should not be included have been included.	Existence: No facts, characteristics which describe facts, parenthetical explanations of facts, relations between facts/characteristics are included within financial report which should not be included.
Inaccuracy: Property of a fact, characteristic, component, or relation is inaccurate. <i>(For example, mathematical relations and model logical structure relations.)</i>	Accuracy: The properties of all facts, characteristics, components, parenthetical explanations, relations between facts/characteristics which are included in the financial report are accurate, correct, and complete.

²⁶ *Financial Report Semantics and Dynamics Theory*, <http://xbrl.squarespace.com/fin-report-sem-dyn-theory/>



Risk	Risk Mitigation Assertion (Verification task)
Infidelity: All facts, characteristics, parenthetical explanations, and relations considered as a whole do not possess the required fidelity when considered as a whole.	Fidelity: Considered as a whole; the facts, characteristics, parenthetical explanations, and relations between facts/characteristics properly reproduces the financial and nonfinancial facts, characteristics, and relations of the reporting entity and provide a true and fair representation of such financial information. Fidelity = faithful representation.
Integrity not intact: Integrity between facts/characteristics is inappropriate.	Integrity: Considered as a whole, the facts and characteristics of those facts reflect the true and proper relations between such facts and characteristics.
Inconsistency: The facts, characteristics, parenthetical explanations, relations and their properties expressed are inconsistent with prior reporting periods or with peers of the reporting entity.	Consistency: The facts, characteristics, parenthetical explanations, relations between facts/characteristics, and their properties are consistent with prior periods and with the reporting entities peers, as is deemed appropriate.
Not presented fairly: The financial report is not presented fairly, in all material respects, and are not a true and fair representation in accordance with the financial reporting framework applied.	True and fair representation: The financial report is a true and fair representation of the information of the reporting entity. An auditor might say presented fairly, in all material respects, and provide a true and fair representation in accordance with the financial reporting framework applied (US GAAP, IFRS, etc.).

3.7. Many aspects of financial reporting are standardized

Financial statement disclosures, in some cases should be a hand-crafted work of art, but not in most cases. Most professional accountants do not desire to be artists; rather they endeavor to comply with financial reporting rules. There are some required disclosures. Other disclosures are required if a reporting entity reports certain specific financial statement line items. Other financial statement disclosures are required if the financial statement line item has certain specific characteristics. Other financial statement disclosures are common practice or purely optional. This information can be organized in different ways. Financial statement disclosures are not random.

As there are price differences between hand-crafted furniture and the furniture which you might purchase at, say, IKEA or at a high end furniture store; there are likewise different prices or costs incurred to taking different approaches to creating financial statement disclosures.

Generally disclosures for financial statement accounts are made if a line item of such account appears on a primary financial statement.

HINT: Jon Rowden and Mike Willis make the following statement in their white paper *Making Sense of XBRL In the US and the UK*²⁷, "The accountants' skill and expertise can then be applied to and focused on disclosures where there is a problem, rather than turning each disclosure note into something resembling the accounting equivalent of a hand-crafted work of art."

²⁷ Making Sense of XBRL in the US and the UK, <http://searchworks.stanford.edu/view/9320284>



Not every part of a financial report needs to be a hand-crafted work of art. Some do. That is where accountants need to spend the majority of their focus.

3.8. *Financial reporting is getting increasingly complex*

Financial reporting is complex and the trend is to become even more complex. Transactions are becoming increasingly complicated, products and services of reporting entities get more and more complex, and financial instruments become more complicated²⁸. Technology can contribute to simplifying financial reporting.

²⁸ *Will simpler also be better?*, <http://www.journalofaccountancy.com/issues/2015/apr/financial-reporting-auditing-complexity.html>

