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Original Paper

Materiality and Relevance in Financial Reporting. Interpretation Problems and Solutions Adopted Internationally.

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Abstract
The concepts of relevance and materiality have, for decades now, been the subject of in-depth study by both doctrine and the bodies whose task it is to issue accounting standards. The aforementioned terms have different meanings in the various countries, although, in general, the difference in interpretation is only a nuance of concept that is often difficult even to identify. When moving from international standards to national standards issued by organisations within individual countries, translation issues can be identified that lead to the use of terms other than relevance and materiality but which, when reading the documents, essentially refer to those standards. As will be seen in the following pages, in Italy these concepts, although identified by different terms than relevance and materiality, have also been adopted by the criminal law concerning evasion and accounting. These concepts therefore transcend the issue of financial reporting to affect both auditing principles and the position of the judiciary, which, applying current legislation, appeals to the tenuity of the fact to reduce or cancel penalties connected with tax offences such as evasion of value added tax.
Keywords
materiality, relevance, GAAP, IAS/IFRS, ISA IFAC, SEC USA

Birth of the Concepts of Materiality and Relevance: Introductory Considerations. (Note)

The concepts of relevance and materiality developed at different times and with different methodologies. In a valuable historical analysis, Holmes (1972) points out how the concept of materiality was introduced in common law for the first time by the English Court in 1867, which used the term material, interpreting it as "relevant and not negligible". Great Britain, therefore, unlike Italy, recognised that no fraud or material error could be permitted in the context of disclosure to third parties. In this regard, however, it may be recalled that, in Italy, even after the 1930s, case law held that it was

impossible to intervene in financial reporting also because it was considered to be an act proper to the directors over which no other power could intervene in any way. Holmes pointed out how, a few years later, in 1895, in deliberation on the British Companies Act, Lord Daney's committee considered highlighting how "every contract or fact is material whichh woulk influence the judgement of a prudent investo in determining whether he would subscribe for the share or debenture offered by the prospectus". (Holmes, 1972).

In the 1930s, after the great crisis, this issue also began to be addressed in the US and the precise concept of materiality was identified. In the SEC, Regulation X-S, 3-06, of 1933, it was stated that "The term "material", when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters as to which an average prudent investor ought reasonably to be informed before purchasing the security registered," (SEC, Regulation S-X, Rule 3-06, 1933). This definition originates from the motivations of the great crisis of 1929. That is, they wanted to give certainty to the average investor so that anyone could, impartially and neutrally, make their own investment decisions. In other words, the intention was to safeguard the vulnerability of investors using a rule that could prevent companies from not providing critical information to third parties outside the company. "The traditional association in professional accounting guidance between materiality and significant errors and omissions for the safety of the reasonable investor, can be traced back to judicial discourses in a landmark UK case, Rex versus Kylsant (1932)". At the heart of the dispute, was the practice of supplementing profit measurement through undisclosed transfers from secret reserves. Reserve accounting was considered prudent (and useful for management) by eminent practitioners (Edwards, 1976). The court viewed the matter from an investor's perspective, where non-disclosure could imply that an investment was safe, when the position was otherwise. In the Court of Criminal Appeal, Mr. Justice Avory stated "the document as a whole may be false not because of what it states, but because of what it does not state, because of what it implies," (Edgley, 2014).

"Although the company auditor was acquitted, the ruling highlighted serious flaws in practitioner judgement (Ashton, 1986). The impact of the case, which Camfferman (1998) has compared to a bomb that disrupted the accountancy world, was interesting in two respects. First, accountants were thereafter expected not just to comply with the law but to use ethical and moral judgement in making materiality decisions. The case reportedly had a greater subsequent impact on audit practices than all previous case law and legislation (Camfferman, 1998). Second, the idea of a material item was extended to omitted data and not just errors (Edwards, 1989). This style of reasoning underpinned the future development of materiality in professional guidance." Edgley (2014).

A precise and unambiguous definition of materiality does not exist. Every accounting body, author, and scholar has illustrated their idea of materiality. Among the explanations that are clearest in interpreting the concept analysed here are those provided by Frishkoff and Kohler's dictionary for accountants in the USA:

Frishkoff stated that " 'Let us define materiality in accounting thus: the relative, quantitative importance of some piece of financial information, to a user, in the context of a decision to be made'. Frishkoff (1970). Inoltre questo autore evidenziava che 'Let us define materiality in accounting thus: the relative, quantitative importance of some piece of financial information, to a user, in the context of a decision to be made'" (Frishkoff, 1970).

In the 1950s, Kohler's dictionary for accountants in the US defined materiality as:

"the characteristic attaching to a statement, fact, or item whereby its disclosure or the method of giving it expression would be likely to influence the judgment of a reasonable person," (Kohler, 1952)

A few years later, the American Accounting Association (AAA) produced the following definition,

Alcuni anni dopo L'associazione AAA identifica il seguente concetto di materiality: "An item should be regarded as material if there is reason to believe that knowledge of it would influence the decisions of an informed investor," (AAA, 1957, p. 8)

In 1967, i.e. a century after the intervention of the English Court, an accounting body, namely the Institute of Chartered Accountants in England and Wales (ICAEW), addressed materiality in more detail with Accounting Recommendation 2.301. The guidance of that accounting body in 1967 stated that "the interpretation of material in relation to accounts….(must be considered...).. in an accounting sense.. a matter is materiali f knoledge of the matter woulk be likely to influence the user of financial or ogher statements under consideration. The use of the word material in relation to accountin matters is inteded to allow scope for differente interpretation accoinding to the variety of circumstances which can arise. It is non possibile or desidderable therefore to give a definition of material in the senso of formula which can be applied mechanically As can be seen, ICAEW, in the recommendation above, points out that the concept of materiality cannot be constrained within a mathematical framework of percentages and must be applied to the economic environment in which it is interpreted".

In the 1970s, various authors attempted to illustrate the concept of materiality in a pragmatic, perhaps unscholarly, but very clear manner. Hicks (1964) stated: "Materiality simply means this: if it doesn't matter, don't bother with it". This author also pointed out that "if financial statements are to be prepared and examined with anything approaching reasonable economy…without such a rule, unwarranted amounts of time would almost certainly be spent on insignificant matters, and financial statements would undoubtedly be cluttered with useless or unimportant information, obscuring the necessary and important facts and relationships they are intended to convey," "To help keep the subject in perspective…the concept is widely and frequently used. For example, when a business executive, applying the technique of "management by exception", cuts through to the matters of significance, he is recognizing materiality. When the president of a corporation, presenting non-financial data in reports to stockholders, prunes away details, he is recognizing materialit "(Hicks, 1964). Mentre Bernstein riteneva che "The concept of materiality is part of the wisdom of life. Its basic meaning is that there is no need to be concerned with what is not important or with what does not matter. Man's work is burdensome enough without his having to pay attention to trivia": (Bernstein, 1973).

In the 1980s, the material concept was often linked to exceeding certain quantitatively determined error thresholds. In this regard, one may recall the statements contained in the principles issued by FASB AND ASB in 1999. "Materiality judgments are concerned with screens or thresholds. Is an item, an error, or an omission large enough, considering its nature and the attendant circumstances, to pass over the threshold that separates material from immaterial items?" (FASB, 1980).

Edgley stated that "materiality was represented in SFAC 2 as a pervasive, base constraint, underpinning all other concepts (FASB, 1980). This involved a consideration of materiality as a buttress for other related concepts, particularly relevance and reliability.[30]

In contrast, the ASB represented materiality, diagrammatically, as a supra threshold, positioned above other concepts. Materiality constituted "the final test" of what information should be included in financial statements (ASB, 1999, paragraph 3.28). The concept was also portrayed as a cut-off point (IASB, 1989) which is a term associated with capital budgeting, risk appraisal and capital investment decisions.

This distinct, scientific territory in discourses has emphasised the importance of an understanding of materiality, as a standardised process, where a foundation for decision-making is neutral. The appeal of science in shaping materiality discourses was probably engendered by auditors as a means of providing evidence to support judgments, rebut criticism and deflect possible problems with litigation." Edgley (2014).

As can be seen, there was no mention of relevance in the various doctrinal and regulatory passages or standards issued by national or international accounting bodies over the past decades. Materiality was the central concept associated with corporate disclosure, and all pragmatic doctrinal and accounting contributions focused on this concept.

In the following pages, it will be seen how, at present, the two concepts coexist: relevance and materiality. However, the clear distinction between the two concepts is not always perceived as, often, the two concepts intersect and overlap, creating not a little confusion for the reader and national translators. They have to translate documents written in English into the local language. From what we will report in the preceding pages, it can see that the concept of materiality is more cited and in-depth than that of relevance, which is relegated to second place even though, as will be shown, the concept of materiality is often understood as a part of the concept of relevance.

After having illustrated the current situation regarding the application of the two concepts of relevance and materiality, it will be possible to consider whether, perhaps, especially in certain documents, it would not be opportune to simplify the issue by merging the two terms and giving the term chosen the meaning of the two concepts mentioned above together.

Materiality and Relevance in IAS/IFRS International Accounting Standards and in ISA (International standard auditing) IFAC n. 320 and n. 450

Nei principi IAS/IFRS vi sono riferimenti sia al concetto di rilevance che al termine di materiality. Analizzando quanto affermato dai principi internazionali si può comprendere come, lo IASB, intenda i due concetti.

Nel Conceptual Framework For Financial Reporting , ai punti 2.4 e 2.5 si afferma:

“**Qualitative characteristics of useful financial information”.**

2.4 If financial information is to be useful, it must be relevant and faithfully represent what it purports to represent. The usefulness of financial information is enhanced if it is comparable, verifiable, timely and understandable.

Fundamental qualitative characteristc

2.5 “The fundamental qualitative characteristics are relevance and faithful representation.”.

In the continuation of the Conceptual Framework, the concept of relevance is explained in more detail. In particular, it states:

Relevance

2.6 Relevant financial information is capable of making a difference in the decisions made by users. Information may be capable of making a difference in a decision even if some users choose not to take advantage of it or are already aware of it from other sources.

2.7 Financial information is capable of making a difference in decisions if it has predictive value, confirmatory value or both.

2.8 Financial information has predictive value if it can be used as an input to processes employed by users to predict future outcomes. Financial information need not be a prediction or forecast to have predictive value. Information with predictive value is employed by users in making their own predictions.

2.9 Financial information has confirmatory value if it provides feedback about (confirms or changes) previous evaluations.

2.10 The predictive value and confirmatory value of financial information are interrelated. Information that has predictive value often also has confirmatory value. For example, revenue information for the current year, which can be used as the basis for predicting revenues in future years, can also be compared with revenue predictions for the current year that were made in past years. The results of those comparisons can help a user to correct and improve the processes that were used to make those previous predictions.

After explaining the concept of relevance, the Conceptual Framework indicates the idea of materiality as a subheading of the idea of relevance. The explanation given is as follows:

“Materiality”

2.11 Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports (see paragraph 1.5) make

on the basis of those reports, which provide financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report.

"Consequently, the Board cannot specify a uniform quantitative threshold for materiality or predetermine what could be material in a particular situation."

From the above, it is clear that in the IAS/IFRS international standards, materiality is a concept included in relevance and has a direct connection to the dimension or context in which relevance is to be applied. For these reasons, the IAS/IFRS international standards deny the possibility of identifying precise materiality thresholds beyond which one must fall, by definition, within the concept of relevance because materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report.

In Chapter 5—Recognition and derecognition, process and criteria, the Conceptual Framework affronta la tematica del recognition process definito come:

"5.1 Recognition is the process of capturing for inclusion in the statement of financial position or the statement(s) of financial performance an item that meets the definition of one of the elements of financial statements—an asset, a liability, equity, income or expenses. Recognition involves depicting the item in one of those statements—either alone or in aggregation with other items—in words and by a monetary amount, and including that amount in one or more totals in that statement. The amount at which an asset, a liability or equity is recognised in the statement of financial position is referred to as its 'carrying amount'."

Also in this Chapter, the Conceptual Framework addresses the issue of relevance by highlighting:

"5.1 Information about assets, liabilities, equity, income and expenses is relevant to users of financial statements. However, recognition of a particular asset or liability and any resulting income, expenses or changes in equity may not always provide relevant information. That may be the case if, for example:

(a) it is uncertain whether an asset or liability exists ;

or

(b) an asset or liability exists, but the probability of an inflow or outflow of economic benefits is low".

In the next point, the Framework specifies that:

"5.13 The presence of one or both of the factors described in paragraph 5.12 does not lead automatically to a conclusion that the information provided by recognition lacks relevance. Moreover, factors other than those described in paragraph 5.12 may also affect the conclusion. It may be a combination of factors and not any single factor that determines whether recognition provides relevant information."

Also in Chapter no. 6, Measurement, il Conceptual Framework highlights the concept of relevance:

Relevance

"6.49 The relevance of information provided by a measurement basis for an asset or liability and for the related income and expenses is affected by:

(a) the characteristics of the asset or liability ;

and

(b) how that asset or liability contributes to future cash flows".

6.50 The relevance of information provided by a measurement basis depends partly on the characteristics of the asset or liability, in particular, on the variability of cash flows and on whether the value of the asset or liability is sensitive to market factors or other risks"

The IASB, in 2017, also issued IFRS Practice Statement 2: Making Materiality Judgements (Practice Statement), which aims to provide operational guidance to financial reporting preparers on the meaning and measurement of the concept of materiality. In this document, it states that The Practice Statement:

- provides an overview of the general characteristics of materiality;
- presents a four-step process companies may follow in making materiality judgements when preparing their financial statements; and
- provides guidance on how to make materiality judgements in specific circumstances; namely, how to make materiality judgements about prior-period information, errors and covenants, and in the context of interim reporting.

The Practice Statement is a non-mandatory document. It does not change or introduce any requirements in IFRS Standards and companies are not required to comply with it to state compliance with IFRS Standards.

In that document, reference is made to both the term relevance and the concept of materiality. But relevance only appears in three passages throughout the document. It is stated that :

"5. Definition of material

Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports make on the basis of those reports, which provide financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report.2"

49. "The relevance of information to the primary users of an entity's financial statements can also be affected by the context in which the entity operates. An external qualitative factor is a characteristic of the context in which the entity's transaction, other event or condition occur that, if present, makes information more likely to influence the primary users' decisions. Characteristics of the entity's context that might represent external qualitative factors include, but are not limited to, the entity's geographical location, its industry sector, or the state of the economy or economies in which the entity operates."

§ 2.11 Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports (see paragraph 1.5) make

on the basis of those reports, which provide financial information about a specific reporting entity. In other words, materiality is an entityspecific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report.

Consequently, the Board cannot specify a uniform quantitative threshold for materiality or predetermine what could be material in a particular situation"

On the other hand, the concept of materiality is the main focus of the entire document, showing that material is a more meaningful term than relevance. It is not possible here to summarise the whole of the document as mentioned above but, to make the reader understand the importance of the concept of material, the following are the main counts expressed in IFRS Practice Statement 2: making materiality judgement:

"IN1 The objective of general purpose financial statements is to provide financial information about a reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity. The entity identifies the information necessary to meet that objective by making appropriate materiality judgements."

IN2 The aim of this IFRS Practice Statement 2 *Making Materiality Judgements* (Practice Statement) is to provide reporting entities with guidance on making materiality judgements when preparing general purpose financial statements in accordance with IFRS Standards. While some of the guidance in this Practice Statement may be useful to entities applying the *IFRS for SMEs*® Standard, the Practice Statement is not intended for those entities.

IN3 The need for materiality judgements is pervasive in the preparation of financial statements. An entity makes materiality judgements when making decisions about recognition and measurement as well as presentation and disclosure. Requirements in IFRS Standards only need to be applied if their effect is material to the complete set of financial statements.

IN4 This Practice Statement:

(a) provides an overview of the general characteristics of materiality.

(b) presents a four step process an entity may follow in making materiality judgements when preparing its financial statements (materiality process). The description of the materiality process provides an overview of the role materiality plays in the preparation of financial statements, with a focus on the factors the entity should consider when making materiality judgements.

(c) provides guidance on how to make materiality judgements in specific circumstances, namely, how to make materiality judgements about priorperiod information, errors and covenants, and in the context of interim reporting.

IN5 Whether information is material is a matter of judgement and depends on the facts involved and the circumstances of a specific entity. This Practice Statement illustrates the types of factors that the entity should consider when judging whether information is material………

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……. **Definition of m aterial**

5 ….Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial reports make on the basis of those reports, which provide financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report.

6 When making materiality judgements, an entity needs to take into account how information could reasonably be expected to influence the primary users of its financial statements—its primary users—when they make decisions on the basis of those statements

…..

8 The need for materiality judgements is pervasive in the preparation of financial statements. An entity makes materiality judgements when making decisions about recognition, measurement, presentation and disclosure. Requirements in IFRS Standards only need to be applied if their effect is material to the complete set of financial statements,6 which includes the primary financial statements 7 and the notes. However, it is inappropriate for the entity to make, or leave uncorrected, immaterial departures from IFRS.

Standards to achieve a particular presentation of its financial position, financial performance or cash flows.

Judgement

11 When assessing whether information is material to the financial statements, an entity applies judgement to decide whether the information could reasonably be expected to influence decisions that primary users make on the basis of those financial statements. When applying such judgement, the entity considers both its specific circumstances and how the information provided in the financial statements responds to the information needs of primary users.

12 Because an entity's circumstances change over time, materiality judgements are reassessed at each reporting date in the light of those changed circumstances.

Decision Make by Primary Users

20 Financial information can make a difference in decisions if it has predictive value, confirmatory value or both. When making materiality judgements, an entity needs to assess whether information could reasonably be expected to influence primary users' decisions, rather than assessing whether that information alone could reasonably be expected to change their decisions.

Intercation wity Local Law and Regulations

27 An entity's financial statements must comply with the requirements in IFRS Standards, including requirements related to materiality (materiality requirements), for the entity to state its compliance with

those Standards. Hence, an entity that wishes to state compliance with IFRS Standards cannot provide less information than the information required by the Standards, even if local laws and regulations permit otherwise.

28 Nevertheless, local laws and regulations may specify requirements that affect what information is provided in the financial statements. In such circumstances, providing information to meet local legal or regulatory requirements is permitted by IFRS Standards, even if that information is not material according to the materiality requirements in the Standards. However, such information must not obscure information that is material according to IFRS Standards.

…..

Overview of the Materiality Process

29 An entity may find it helpful to follow a systematic process in making materiality judgements when preparing its financial statements. The four step process described in the following paragraphs is an example of such a process. This description provides an overview of the role materiality plays in the preparation of financial statements, with a focus on the factors the entity should consider when making materiality judgements. In this Practice Statement, this fourstep process is called the 'materiality process'.

30 The materiality process describes how an entity could assess whether information is material for the purposes of presentation and disclosure, as well as for recognition and measurement. The process illustrates one possible way to make materiality judgements, but it incorporates the materiality requirements an entity must apply to state compliance with IFRS Standards. The materiality process considers potential omission and potential misstatement of information, as well as unnecessary inclusion of immaterial information and whether immaterial information obscures material information. In all cases, the entity needs to focus on how the information could reasonably be expected to influence decisions of the primary users of its financial statements.

31 Judgement is involved in assessing materiality when preparing financial statements. The materiality process is designed as a practice guide to help an entity apply judgement in an efficient and effective way.

32 The materiality process is not intended to describe the assessment of materiality for local legal and regulatory purposes. An entity refers to its local requirements to assess whether it is compliant with local laws and regulations.

A Four-Step Materiality Process

33 The steps identified as a possible approach to the assessment of materiality in the preparation of the financial statements are, in summary:

(a) Step 1—identify. Identify information that has the potential to be material.

(b) Step 2—assess. Assess whether the information identified in Step 1 is, in fact, material.

(c) Step 3—organise. Organise the information within the draft financial statements in a way that communicates the information clearly and concisely to primary users.

(d) Step 4—review. Review the draft financial statements to determine whether all material information has been identified and materiality considered from a wide perspective and in aggregate, on the basis of the complete set of financial statements.

34 When preparing its financial statements, an entity may rely on materiality assessments from prior periods, provided that it reconsiders them in the light of any change in circumstances and of any new or updated information.

…….

Interaction of Qualitative and Quantitative Factors

52 An entity could identify an item of information as material on the basis of one or more materiality factors. In general, the more factors that apply to a particular item, or the more significant those factors are, the more likely it is that the item is material.

53 Although there is no hierarchy among materiality factors, assessing an item of information from a quantitative perspective first could be an efficient approach to assessing materiality. If an entity identifies an item of information as material solely on the basis of the size of the impact of the transaction, other event or condition, the entity does not need to assess that item of information further against other materiality factors. In these circumstances, a quantitative threshold—a specified level, rate or amount of

one of the measures used in assessing size—can be a helpful tool in making a materiality judgement. However, a quantitative assessment alone is not always sufficient to conclude that an item of information is not material. The entity should further assess the presence of qualitative factors.

54 The presence of a qualitative factor lowers the thresholds for the quantitative assessment. The more significant the qualitative factors, the lower those quantitative thresholds will be. However, in some cases an entity might decide that, despite the presence of qualitative factors, an item of information is not material because its effect on the financial statements is so small that it could not reasonably be expected to influence primary users' decisions.

Organise

56 Classifying, characterising and presenting information clearly and concisely makes it understandable.23 An entity exercises judgement when deciding how to communicate information clearly and concisely. For example, the entity is more likely to clearly and concisely communicate the material information identified in Step 2 by organising it to:

(a) emphasise material matters;

(b) tailor information to the entity's own circumstances;

(c) describe the entity's transactions, other events and conditions as simply and directly as possible without omitting material information and without unnecessarily increasing the length of the financial statements;
(d) highlight relationships between different pieces of information;
(e) provide information in a format that is appropriate for its type, eg tabular or narrative;
(f) provide information in a way that maximises, to the extent possible, comparability among entities and across reporting periods;
(g) avoid or minimise duplication of information in different parts of the financial statements; and
(h) ensure material information is not obscured by immaterial information.
57 Financial statements are less understandable for primary users if information is organised in an unclear manner. Similarly, financial statements are less understandable if an entity aggregates material items that have different natures or functions, or if material information is obscured,24 for example, by an excessive amount of immaterial information.
….

Errors

72 Errors are omissions from and/or misstatements in an entity's financial statements arising from a failure to use, or misuse of, reliable information that is available, or could reasonably be expected to be obtained. Material errors are errors that individually or collectively could reasonably be expected to influence decisions that primary users make on the basis of those financial statements. Errors may affect narrative descriptions disclosed in the notes as well as amounts reported in the primary financial statements or in the notes.
73 An entity must correct all material errors, as well as any immaterial errors made intentionally to achieve a particular presentation of its financial position, financial performance or cash flows, to ensure compliance with IFRS Standards.36 The entity should refer to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* for guidance on how to correct an error.
74 Immaterial errors, if not made intentionally to achieve a particular presentation, do not need to be corrected to ensure compliance with IFRS Standards. However, correcting all errors (including those that are not material) in the preparation of the financial statements lowers the risk that immaterial errors will accumulate over reporting periods and become material.
75 An entity assesses whether an error is material by applying the same considerations as outlined in the description of the materiality process. Making materiality judgements about errors involves both quantitative and qualitative considerations. The entity identifies information that, if misstated or omitted, could reasonably be expected to influence primary users' decisions (as described in Step 1 and Step 2 of the materiality process). The entity also considers whether any identified errors are material on a collective basis (as described in Step 4 of the materiality process).
76 If an error is judged not to be material on its own, it might be regarded as material when considered in combination with other information. However, in general, if an error is individually assessed as

material to an entity's financial statements, the existence of other errors that affect the entity's financial position, financial performance or cash flows in the opposite way, does not make the error immaterial, nor does it eliminate the need to correct the error".

This summary of IFRS Practice Statement 2: making materiality judgement makes it clear that the concept of materiality overpowers that of relevance, which, although mentioned, plays a decidedly less relevant role than materiality. Although in pragmatic terms, it is often noted that materiality is a part of relevance, the lack of a focus on relevance, compared to the analytical focus on materiality, one may wonder whether the time has not come to simplify the terminology used. The concepts referred to by seeking a broad term that encompasses the two concepts also considering the circumstance that, in essence, since the one is a part of the other (as much as this is stated in many official documents), it would be simpler and clearer to use a single term that encompasses the two concepts. This is also because the two words are often misinterpreted or simplified in the translation of local unique. In this regard, the reader is referred to the Italian situation where, in national accounting standards, there is only one term: relevance. This term, however, clearly refers to what is meant by materiality in English-language documents. And also, considering the confusion in the translation of certain documents, such as, for example, Legislative Decree No. 254 of 30 December 2016, which regulates non-financial information and which derives, in part, from the at least confusing translation of the relevance and materiality of the term identified in the EU directive from which this decree originates (Directive 2014/95/2014).

In ISA IFAC Principles Nos. 320 and 450, there is no reference to the principle of relevance while much space is given to the concept of materiality.

In particular, ISA IFAC Standard No. 320 points out that: **"Scope of this ISA"**

1 This International Standard on Auditing (ISA) deals with the auditor's responsibility to apply the concept of materiality in planning and performing an audit of financial statements. ISA 4501 explains how materiality is applied in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements.

Materiality in the Context of an Audit

2. Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of financial statements. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that:

• Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements;

• Judgments about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and

• Judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.

3. Such a discussion, if present in the applicable financial reporting framework, provides a frame of reference to the auditor in determining materiality for the audit. If the applicable financial reporting framework does not include a discussion of the concept of materiality, the characteristics referred to in paragraph 2 provide the auditor with such a frame of reference.

4. The auditor's determination of materiality is a matter of professional judgment, and is affected by the auditor's perception of the financial information needs of users of the financial statements. ….

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6. In planning the audit, the auditor makes judgments about the size of misstatements that will be considered material. These judgments provide a basis for:

(a) Determining the nature, timing and extent of risk assessment procedures;

(b) Identifying and assessing the risks of material misstatement; and

(c) Determining the nature, timing and extent of further audit procedures.

The materiality determined when planning the audit does not necessarily establish an amount below which uncorrected misstatements, individually or in the aggregate, will always be evaluated as immaterial. The circumstances related to some misstatements may cause the auditor to evaluate them as material even if they are below materiality. Although it is not practicable to design audit procedures to detect misstatements that could be material solely because of their nature, the auditor considers not only the size but also the nature of uncorrected misstatements, and the particular circumstances of their occurrence, when evaluating their effect on the financial statements

Definition

9. For purposes of the ISAs, performance materiality means the amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. If applicable, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for particular classes of transactions, account balances or disclosures.

…

Application and Other Explanatory Materia

Materiality and Audit Risk

A1. In conducting an audit of financial statements, the overall objectives of the auditor are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on

whether the financial statements are prepared, in all material respects, in accordance with an applicable financial reporting framework; and to report on the financial statements, and communicate as required by the ISAs, in accordance with the auditor's findings. 5 The auditor obtains reasonable assurance by obtaining sufficient appropriate audit evidence to reduce audit risk to an acceptably low level.6 Audit risk is the risk that the auditor expresses an inappropriate audit opinion when the financial statements are materially misstated. Audit risk is a function of the risks of material misstatement and detection risk.7 Materiality and audit risk are considered throughout the audit, in particular, when:

(a) Identifying and assessing the risks of material misstatement;

(b) Determining the nature, timing and extent of further audit procedures;

(c) Evaluating the effect of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report.

Use of Benchmarks in Determining Materiality for the Financial Statements as a Whole

A3. Determining materiality involves the exercise of professional judgment. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. Factors that may affect the identification of an appropriate benchmark include the following:

• The elements of the financial statements (for example, assets, liabilities, equity, revenue, expenses);

• Whether there are items on which the attention of the users of the particular entity's financial statements tends to be focused (for example, for the purpose of evaluating financial performance users may tend to focus on profit, revenue or net assets);

• The nature of the entity, where the entity is in its life cycle, and the industry and economic environment in which the entity operates;

• The entity's ownership structure and the way it is financed (for example, if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings); and

The relative volatility of the benchmark.

...

Performance Materiality

A12. Planning the audit solely to detect individually material misstatements overlooks the fact that the aggregate of individually immaterial misstatements may cause the financial statements to be materially misstated, and leaves no margin for possible undetected misstatements. Performance materiality (which, as defined, is one or more amounts) is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements as a whole. Similarly, performance materiality relating to a materiality level determined for a particular class of transactions, account balance or disclosure is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in that particular class of transactions, account balance or disclosure exceeds the

materiality level for that particular class of transactions, account balance or disclosure. The determination of performance materiality is not a simple mechanical calculation and involves the exercise of professional judgment. It is affected by the auditor's understanding of the entity, updated during the performance of the risk assessment procedures; and the nature and extent of misstatements identified in previous audits and thereby the auditor's expectations in relation to misstatements in the current period.

As can be seen from the above summary, the concept of materiality is analysed in great detail, while the term relevance does not appear in ISA IFAC Document 320.

A similar situation occurs in the International Standard on Auditing ISA IFAC 450 Evaluation of Misstatements identified during the audit. Not even in this document is there any reference to the concept of relevance while there are numerous references to materiality. In a nutshell, ISA IFAC 450 highlights:

"**Scope of this ISA**"

1. This International Standard on Auditing (ISA) deals with the auditor's responsibility to evaluate the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements. ISA 700 deals with the auditor's responsibility, in forming an opinion on the financial statements, to conclude whether reasonable assurance has been obtained about whether the financial statements as a whole are free from material misstatement. The auditor's conclusion required by ISA 700 takes into account the auditor's evaluation of uncorrected misstatements, if any, on the financial statements, in accordance with this ISA.1 ISA 3202 deals with the auditor's responsibility to apply the concept of materiality appropriately in planning and performing an audit of financial statements.

……

Consideration of Identified Misstatements as the Audit Progresses

6. The auditor shall determine whether the overall audit strategy and audit plan need to be revised if:

(a) The nature of identified misstatements and the circumstances of their occurrence indicate that other misstatements may exist that, when aggregated with misstatements accumulated during the audit, could be material; or

(b) The aggregate of misstatements accumulated during the audit approaches materiality determined in accordance with ISA 320.

Evaluating the Effect of Uncorrected Misstatements

10. Prior to evaluating the effect of uncorrected misstatements, the auditor shall reassess materiality determined in accordance with ISA 320 to confirm whether it remains appropriate in the context of the entity's actual financial results.

11. The auditor shall determine whether uncorrected misstatements are material, individually or in aggregate. In making this determination, the auditor shall consider:

(a) The size and nature of the misstatements, both in relation to particular classes of transactions, account balances or disclosures and the financial statements as a whole, and the particular circumstances of their occurrence; and
(b) The effect of uncorrected misstatements related to prior periods on the relevant classes of transactions, account balances or disclosures, and the financial statements as a whole.

Accumulation of Identified Misstatements
A2. The auditor may designate an amount below which misstatements would be clearly trivial and would not need to be accumulated because the auditor expects that the accumulation of such amounts clearly would not have a material effect on the financial statements. "Clearly trivial" is not another expression for "not material." Matters that are clearly trivial will be of a wholly different (smaller) order of magnitude than materiality determined in 5 ISA 230 and will be matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any criteria of size, nature or circumstances. When there is any uncertainty about whether one or more items are clearly trivial, the matter is considered not to be clearly trivial.

Evaluating the Effect of Uncorrected Misstatements
A11. The auditor's determination of materiality in accordance with ISA 320 is often based on estimates of the entity's financial results, because the actual financial results may not yet be known. Therefore, prior to the auditor's evaluation of the effect of uncorrected misstatements, it may be necessary to revise materiality determined in accordance with ISA 320 based on the actual financial results.
A12. ISA 320 explains that, as the audit progresses, materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances or disclosures) is revised in the event of the auditor becoming aware of information during the audit that would have caused the auditor to have determined a different amount (or amounts) initially. 10 Thus, any significant revision is likely to have been made before the auditor evaluates the effect of uncorrected misstatements. However, if the auditor's reassessment of materiality determined in accordance with ISA 320 gives rise to a lower amount (or amounts), then performance materiality and the appropriateness of the nature, timing and extent of the further audit procedures are reconsidered so as to obtain sufficient appropriate audit evidence on which to base the audit opinion.
A13. Each individual misstatement is considered to evaluate its effect on the relevant classes of transactions, account balances or disclosures, including whether the materiality level for that particular class of transactions, account balance or disclosure, if any, has been exceeded.
A14. If an individual misstatement is judged to be material, it is unlikely that it can be offset by other misstatements. For example, if revenue has been materially overstated, the financial statements as a whole will be materially misstated, even if the effect of the misstatement on earnings is completely offset by an equivalent overstatement of expenses. It may be appropriate to offset misstatements within

the same account balance or class of transactions; however, the risk that further undetected misstatements may exist is considered before concluding that offsetting even immaterial misstatements is appropriate.

A15. Determining whether a classification misstatement is material involves the evaluation of qualitative considerations, such as the effect of the classification misstatement on debt or other contractual covenants, the effect on individual line items or sub-totals, or the effect on key ratios. There may be circumstances where the auditor concludes that a classification misstatement is not material in the context of the financial statements as a whole, even though it may exceed the materiality level or levels applied in evaluating other misstatements. For example, a misclassification between balance sheet line items may not be considered material in the context of the financial statements as a whole when the amount of the misclassification is small in relation to the size of the related balance sheet line items and the misclassification does not affect the income statement or any key ratios.

A16. The circumstances related to some misstatements may cause the auditor to evaluate them as material, individually or when considered together with other misstatements accumulated during the audit, even if they are lower than materiality for the financial statements as a whole….”

From the above summaries of the IFAC ISA principles, it can be seen that relevance appears sporadically in the ISAs while materiality is very thorough.

3) Materiality and relevance in Italian Accounting Standard and Italian audit Standard: non-existent differentiation

In the Italian Civil Code, there is no differentiation between the concept of relevance and materiality. Article 2423(4) of the Italian Civil Code states that “there is no need to comply with recognition, measurement, presentation and disclosure requirements when their observance would have an insignificant effect on the true and fair view. Obligations regarding the regular maintenance of accounting records remain unaffected. Companies shall explain in the notes to the financial statements the criteria by which they have implemented this provision”.

The relevance principle is addressed in the Italian national accounting standards OIC No. 11 Purposes and Postulates of Financial Reporting and No. 29 Changes in Accounting Policies, Changes in Accounting Estimates, Correction of Errors, Events Occurring After the End of the Financial Year.

In the Italian national standard OIC No. 11 (Italian Accounting Standards Board), Purposes and Postulates of Financial Reporting, a part of the standard is dedicated to relevance. However, the term materiality is not found in standard No. 11. From this, it can deduce that no differentiation is made between the concept of relevance and materiality in OIC Principle No. 11. Therefore, in the Italian OIC accounting standards, the relevance concept does not coincide with that used in English-language documents. In essence, in the Italian documents, the only idea presents its relevance. In the absence of any reference to materiality and considering the definitions attributed to this concept, it is evident how

it encompasses both the idea of relevance and materiality. The OIC Principle No. 11 Purposes and Postulates of Financial Reporting defines what it calls relevance in the following terms:

Relevance

The concept of materiality is pervasive in the financial reporting process. 36. Information is considered material when its omission or misstatement could reasonably be expected to influence the decisions made by the primary recipients of the financial reporting based on the company's financial reporting. The materiality of individual items of financial reporting is judged in the context of the company's financial position, results of operations and financial situation.

37. Both qualitative and quantitative elements are considered in quantifying materiality.

38. Quantitative factors consider the magnitude of the economic effects of the transaction or other events concerning the financial statement amounts. Identifying the financial reporting values used to determine materiality is an evaluative process that may vary from case to case. In any case, priority should be given to the financial reporting items of most interest to the primary recipients of the financial statements.

39. Qualitative factors per se transcend quantitative aspects because they relate to particular characteristics of the transaction or event, the importance of which is that it could reasonably influence the economic decisions of the primary recipients of the entity's financial reporting.

40. Paragraph 4 of Article 2423 of the Civil Code provides that there is no need to comply with recognition, measurement, presentation and disclosure requirements when compliance with them would have an immaterial effect on giving a true and fair view. Obligations 12 regarding the regular maintenance of accounting records remain unaffected. Companies shall explain in the notes to the financial statements the criteria by which they have implemented this provision.

41. Accordingly, the legal prerequisite for the obligation to provide specific information in the notes is a conscious decision to depart from a stated accounting rule, provided that the effects of the departure are immaterial. The preparer of the financial statements, in giving an account in the notes to the financial statements of his accounting policies and, in particular, of the concrete methods of applying the accounting principles to his company, must also highlight the application methods referring to the faculty of the derogation provided for in paragraph 4 of Article 2423 of the Civil Code.

42. The national accounting standards provide, by way of example and not as an exhaustive list, some examples of cases in which it is possible to depart from an accounting rule, provided that the departure would have immaterial effects. For example, a company required to apply the amortised cost criterion may decide not to use it for receivables or payables with a maturity of fewer than 12 months or not to discount a receivable or payable if the interest rate inferable from the contractual terms is not significantly different from the market interest rate.

To explain the rationale for this definition, OIC Standard No. 11 highlights some interesting observations:

Relevance

18. Under OIC 11, information is regarded as material when its omission or misstatement could reasonably be expected to influence the decisions made by the primary recipients of the financial reporting information. In addition, the materiality of individual items of financial reporting is judged in the overall context of the financial statements.

19. The definition of materiality is based on Directive 2013/34/EU, according to which materiality is: "the state of information when its omission or misstatement could reasonably be expected to influence the decisions made by users based on the financial reporting of the company. The materiality of individual items is judged in the context of other similar items. Concerning this definition, the interpretative elements are a) the identification of the 'primary' users of the financial reporting information, which will discuss below; b) the reference to the materiality of the items composing the financial reporting items concerning the financial reporting as a whole, and not to the context of similar items. This choice is because the reference to other similar items is not apparent in the Directive's wording. Thus, the preparer of financial reporting assesses the materiality of the individual item by reference to financial reporting as a whole, and not its materiality within an individual item".

20. A central element of the definition concerns the identification of the recipients of the financial statements. Two approaches were possible here: (i) to speak generically of addressees; or (ii) to introduce a hierarchy of addressees (primary, secondary, etc.)

21. Concerning materiality, the problem arises in guiding the definition of the materiality threshold according to parameters that are not merely discretionary. The first option offers a wide range of recipients of financial reporting that could lead to application difficulties. Indeed, the more indistinct the set of recipients, the more difficult it is to determine what is material or not. Consider the case in which a piece of information deemed by the company irrelevant for the generality of investors is essential for some external, non-investor stakeholders. The omission of such information could result in an incorrect application of the concept of materiality.

22. It adopted the second option by introducing the category of primary recipients, defining them as those who provide financial resources to the company: investors, lenders and other creditors. This approach enables the preparer to define more precisely the information needs that financial reporting must satisfy and allows the relevance of the information to be established more objectively. Finally, it should emphasise that, in most cases, helpful information to primary recipients also meets the information needs of other non-priority users.

23. The IAS/IFRS definition of materiality also provides for the hierarchical approach of primary recipients. The convergence on this point between national accounting standards and IAS/IFRS does not seem without utility. It would not be acceptable to circumscribe the scope of recipients for listed companies and maintain an indeterminate range for less structured companies.

24. OIC 11 also provides for how information is to be provided in the notes on the criteria used to implement the provision of Article 2423(4) of the Civil Code on the possibility of exemption from the

recognition, measurement, presentation and disclosure requirements in the case of immateriality. 25. Considering that this is a disclosure requirement not provided for by Directive 2013/34/EU, it seemed appropriate to require the inclusion of the information in question in the part of the notes to the financial statements intended to describe the accounting policies followed. The cases provided in this regard in the OICs are not exhaustive. After all, it may well be that the exemption is also applied in other cases because, in that case, it is considered by the preparer of the financial reporting irrelevant for true and fair representation.

The analysis of what has been stated in paragraph no. 23 above makes it clear how in OIC principle no. 11, the concepts of relevance and materiality are considered as synonyms or, in any case, as alternative terms that, in substance, indicate the same basic concept. For this reason, it can be said that in Italian accounting standards, there is no real distinction between the concept of materiality and relevance.

Even in the national standard OIC No. 29, Changes in Accounting Principles, Changes in Accounting Estimates, Correction of Errors, Events Occurring After the End of the Financial Year, it can be seen that the term relevance appears. Still, there is no reference to the concept of materiality.

In particular, this standard states that :

"CORRECTIONS OF ERRORS"

44. An error is the improper or non-application of an accounting policy if the information and data necessary for its proper application are available at the time it is made. Errors may occur because of mathematical mistakes, misinterpretations of facts, or negligence in gathering the information and data available for proper accounting treatment.

45. Errors should not be confused with changes in estimates or accounting policies, both of which are different. In particular, the following do not constitute errors: a. changes that subsequently prove necessary in judgements and estimates that were made based on information and data available at the time; or b. the adoption of accounting policies that were made based on information and data available at the time but subsequently prove to be different from those underlying the choice made if, in either case, such information and data were collected and used with due care at the time them.

46. An error is material if it could individually, or together with other mistakes, influence the economic decisions that users make based on the financial statements. The materiality of an error depends on the size and nature and is assessed in the circumstances.

47. A correction of an error shall be recognised in financial reporting when the error is identified, and at the same time, information and data are available for its proper treatment.

48. The correction of material errors made in prior periods is recognised in the opening balance of equity in the period in which the error is identified. Usually, the discipline is recognised in retained earnings. However, the adjustment may be made to another equity component if more appropriate. The modification of immaterial errors made in prior years is recognised in the year's income statement in which the error is identified.

49. Except as provided in paragraph 50, an entity shall, for comparative purposes only, correct material errors made in prior periods retrospectively in the first financial report after they are identified as follows: a. if the mistake was made in the preceding period, restating the comparative amounts for the prior period; or b. if the error was made before the beginning of the preceding period, restating the opening balances of assets, liabilities and equity for the prior period.
50. A material error made in a prior period shall be corrected by retrospectively restating comparative information, except when it is impracticable to determine either the prior period's effect or the cumulative effect of the error.
51. When it is impracticable to determine the prior period effect of a material error, the entity shall restate the opening balance of assets, liabilities and equity for the current period. Again, the correction of material errors made in prior periods is made to the opening balance of equity for the period in which the error is identified.
55. Article 2423-ter of the Civil Code provides that 'if items are not comparable, it shall adjust those of the previous year; the non-comparability and the adjustment or impossibility thereof shall be disclosed and commented on in the notes to the financial statements. Thus, in the case of material errors made in prior periods, the notes to the financial statements shall disclose: - a description of the error made; - the amount of the correction made for each item in the balance sheet and income statement concerned; and - the reasons for the use of the facilities granted by paragraphs 51 and 52.
As can be seen, not even in OIC Standard No. 29 can the coexistence of the two terms' relevance and materiality be identified? All the Italian national standards speak of relevance, meaning, at the same time, what is often placed in English-language documents, as we shall see later, sometimes with the concept of relevance and sometimes with the term materiality.
The demonstration that the concepts of relevance and materiality are not part of Italian culture and that, consequently, the translation of documents written in the English language is marked by terms that do not coincide with the two aforementioned concepts can also be found in the translation of the ISA Italia principles, which are derived from the Italian translation of the ISA IFAC principles.
In these ISA Italia principles, the concepts of relevance and materiality are replaced by the only term we can refer to in English as meaningfulness which, of course, includes both the concept of relevance (present, in fact, only three times in ISA IFAC principle 320) and materiality. However, it should note that in a document issued by the National Council of Chartered Accountants, Quality Challenge Working Group, Document: Methodological Approach to Statutory Auditing in Smaller Firms.
In that document, it is stated that "The concept of meaningfulness ('materiality' in the Anglo-Saxon world) is applied in auditing both in the planning and execution phases of the work, as well as in the assessment of the effects, including omissions; it is, therefore, a key concept in all phases of auditing, so much so that the entire international auditing standard ISA Italia 320, 'meaningfulness in planning and performing audits', has been dedicated to it.

As a first approximation, as generally clarified by the systematic frameworks for preparing and presenting financial information in the context of financial reporting.

- errors are considered material when they can 'reasonably be expected, taken individually or as a whole, to influence the economic decisions taken by users based on the financial statements;
- judgements about meaninglulness are made by the auditor in light of contingent circumstances and influenced by the magnitude and nature of the error or a combination of both;
- judgements on matters meaningful to users of financial reporting are based on consideration of users' standard financial reporting needs as a group; the possible effect of errors on specific individual users, whose needs may vary considerably, is not considered.

The auditor's determination of meaningfulness is, therefore, a matter of professional judgement, formulated in the light of contingent circumstances and influenced by the magnitude and nature of the error, or a combination of both, and nonetheless by the auditor's perception of the financial reporting needs of the users of financial reporting as identified above. The concept of meaningfulness is the auditor's guide through all stages of the process because it must apply it

- first, at the planning stage of the work and the related controls and checks
- during the execution of the same;

Finally, in assessing the effect of identified errors and the effect of uncorrected errors on financial reporting and consequently in forming the opinion expressed in the audit report.

Meaningfulness does not, therefore and exclusively, consist of a point value. Instead, it consists of, the undefined area between what is most probably not significant and what is most probably important, i.e., it could also consist of a more or less wide range of values'.

Within the auditing principles in ISA Italy IFAC, the Consiglio Nazionale Dottori Commercialisti e Esperti Contabili, together with IFAC, decided to highlight concepts not present in the ISA IFAC documents regarding meaningfulness. In particular, meaningfulness in Italy has been divided into four sub-concepts: general meaningfulness: and general meaningfulness refers to financial reporting as a whole. It is based on what could reasonably be expected to influence the economic decisions of users taken based on the financial statements. It will be changed during the audit if the auditor becomes aware of information that would have led him to determine a different amount from the outset.

General operational meaningfulness is set at a lower level than general point meaningfulness. Operational meaningfulness allows the auditor to respond to specific risk assessments without changing the general point meaningfulness and to reduce to an appropriately low level the likelihood that the set of uncorrected errors not identified on the general point meaningfulness operational meaningfulness will be changed based on audit findings, for example when the risk assessment has been modified.

specific meaningfulness is determined for classes of transactions, account balances or disclosures when errors of less than general meaningfulness could reasonably be expected to influence the economic decisions that users make based on the financial statements:

specific operational meaningfulness: specific operational meaningfulness and stability at a lower level than specific meaningfulness. This allows the auditor to respond to specific risk assessments and to disallow the existence of undetected and individually insignificant errors that, cumulatively, are not material.

The ‘meaningfulness for the financial reporting as a whole’ indicates the numerical value above which the auditor assesses the impact of any identified errors (individually or in the aggregate) on its assessment. Such meaningfulness can be identified using various methodologies that have been developed mainly by Anglo-Saxon or US-based doctrine. The most commonly used methods are:

- the criterion linked to the company’s size factor
- the average criterion
- the mathematical formula criterion
- the general criterion, i.e. the so-called ‘rule of thumb’.

The Consiglio Nazionale Dottori Commercialisti e Esperti Contabii suggests referring to the last-mentioned method. In particular, meaningfulness is determined by referring to the percentages of individual balance sheet items. These percentages have been defined using the IFAC guides as a reference.

The IFAC ISA Guide suggests using the following financial reporting parameters:

reference value	
revenues	1% - 3%
Operating profit	3%-7%
Total assets	1%-3%
equity	3%-5%

ISA Italy Standard 320, on general meaningfulness, states that :

“2. Financial reporting frameworks often address the concept of meaningfulness in financial statement preparation. Although financial reporting frameworks may treat meaningfulness in different terms, they generally make clear that:

- errors, including omissions, are considered material if they could reasonably be expected, taken individually or as a whole, to influence the economic decisions made by users based on the financial statements;
- judgments about materiality are made in the light of contingent circumstances and are influenced by the extent or nature of an error, or a combination of both;
- judgements on material matters to users of the financial report are based on consideration of the common financial reporting needs of users as a group.

The possible effect of errors on specific individual users, whose needs may vary considerably, is not considered.

3. Such treatment, if present in the applicable financial reporting framework, provides the auditor with a framework for determining the meaningfulness of the audit. Where the appropriate financial reporting framework does not provide for a discussion of meaningfulness, the guidance referred to in paragraph 2 provides the auditor with a framework.

4. The auditor's determination of meaningfulness is a matter of professional judgement and is influenced by the auditor's perception of the financial reporting needs of users of financial statements.

Of the users of the financial statements. In this context, it is reasonable for the auditor to assume that the users:

(a) have a reasonable knowledge of the business and economic activities and accounting and a willingness to review the information in the financial statements with reasonable diligence;

(b) understand that the financial reporting is prepared and audited to a level of meaningfulness;

(c) recognise the inherent uncertainties in quantifying amounts based on the use of estimates, subjective judgments and the consideration of future events;

(d) make reasonable economic decisions based on the information in the financial statements.

5. The concept of meaningfulness is applied by the auditor both in planning and performing the audit and in assessing the effect of identified errors on the conduct of the audit and the effect of uncorrected errors, if any, on the financial statements, as well as in forming an opinion in the audit report.

6. In planning the audit, the auditor applies their professional judgement to determine the errors that will be considered material. Such assessment provides a basis for:

(a) determining the nature, timing and extent of risk assessment procedures;

(b) identifying and assessing the risks of significant errors;

(c) establishing the nature, timing and extent of subsequent audit procedures.

The meaningfulness determined during audit planning does not necessarily establish an amount below which uncorrected errors, taken individually or as a whole, will continually be assessed as not material. The circumstances surrounding some errors may lead the auditor to evaluate them as significant even though they are below meaningfulness. It is not feasible to establish audit procedures to identify all mistakes that could be significant solely because of their nature. However, consideration of the nature of potential errors in the disclosures is relevant to the definition of audit procedures to address the risks of material misstatement. Furthermore, in assessing the effectiveness of all uncorrected mistakes on the financial statements, the auditor considers the magnitude and nature of the uncorrected errors and the particular circumstances in which they occur".

Concerning operational meaningfulness, ISA Italy Standard 320 emphasises that.

"9. For auditing standards, operational meaningfulness for the audit refers to the amount or amounts set by the auditor below the meaningfulness for financial reporting to reduce to an appropriately low level the likelihood that the set of uncorrected and undetected errors exceeds the meaningfulness for

financial reporting as a whole. Where applicable, operational meaningfulness for the audit also refers to the amount(s) determined by the auditor to be less than the level(s) of meaningfulness for particular classes of transactions, balances or disclosures.

10. In setting the overall audit strategy, the auditor shall determine the meaningfulness of financial reporting. Suppose, in the specific circumstances of the enterprise; there are one or more particular classes of transactions, balances or disclosures for which errors of less than the meaningfulness considered for financial reporting as a whole could reasonably be expected to influence the economic decisions made by users based on the financial statements. In that case, the auditor shall also determine the level or levels of meaningfulness to be applied to those particular classes of transactions, balances or disclosures.

11. The auditor should determine the operational meaningfulness of the audit in assessing the risks of material misstatement and in determining the nature, timing and extent of the resulting audit procedures.

12. The auditor shall adjust the meaningfulness for financial reporting as a whole (and, where applicable, the level(s) of meaningfulness for classes of transactions, account balances, or disclosures) if, during the audit, information becomes known that would have led the auditor to determine a different amount(s) from the outset.

13. If the auditor concludes that a lower level of meaningfulness for financial reporting as a whole (and, where applicable, the level(s) of meaningfulness for particular classes of transactions, account balances or disclosures) than initially determined is appropriate, the auditor shall determine whether it is necessary to change the operational meaningfulness for the audit and whether the nature, timing and extent of the resulting audit procedures continue to be appropriate."

ISA Italy 320 also points out that:

"A13. In planning an audit solely to identify individually

In planning an audit solely to identify individually significant errors, one overlooks that a set of mistakes, which individually are not substantial, may render financial reporting materially misleading, leaving no room for possible undetected errors. Operational meaningfulness for audit (which, as defined, is represented by one or more amounts) is determined to reduce to an appropriately low level the probability that the set of uncorrected and undetected errors in the financial report exceeds the meaningfulness for financial reporting as a whole. Similarly, operational meaningfulness for the audit, relative to a level of meaningfulness established for a particular class of transaction, account balance or disclosure,

determined to reduce to an appropriately low level the probability that the set of uncorrected and undetected errors in that particular class of transactions, account balances or disclosures exceeds the relevant level of meaningfulness. The determination of operational meaningfulness for the audit is not a simple mechanical calculation and requires the exercise of professional judgement. It is influenced by the auditor's understanding of the business, as updated in the course of conducting risk assessment

procedures, by the nature and extent of errors identified in previous audits, and thus by the auditor's expectations of the errors in the reporting period."

The professional practice referred to in ISA Italia determines operational meaningfulness, usually within 60% to 85% of meaningfulness for financial reporting as a whole. However, as ISA Italia 320 emphasises, "the determination of operational meaningfulness for auditing is not a simple mechanical calculation and requires the exercise of professional judgement".

Concerning specific meaningfulness, in the guidance issued by the Italian National Council of Chartered Accountants and IFAC on practical guidelines to be followed in the corporate audit of small and medium-sized enterprises, it is noted that this concept is related to the occurrence of specific situations in which errors below the level of general meaningfulness could reasonably be expected to influence the economic decisions of users taken based on the financial statements.

By way of example, the National Council of Accountants document lists the following cases:

*disclosure in financial reporting of sensitive information, e.g. remuneration of management and governance

*transactions with related parties

*non-compliance with loan covenants, contractual agreements, laws and regulations, financial reporting

*certain types of expenses such as improper payments or fees incurred by management

*inventory and exploration costs for a mining company

*research and development costs for a pharmaceutical company

*recent acquisitions or expansions of operations

*discontinued operations

*unusual events or circumstances such as lawsuits

*introduction of new products or services.

Finally, the guidance issued by Italian National Council of Chartered Accountants on ISA Italy provides the following definition of specific operational meaningfulness: "this is the same as the operational meaningfulness discussed above except that it relates to the levels set for specific meaningfulness. The specific operational meaningfulness will be set at a lower amount than the specific meaningfulness to ensure that sufficient audit work is performed to reduce the probability that the set of uncorrected and undetected errors exceeds the specific meaningfulness to an appropriately low level".

From the above, it can understand how, in the ISA Italia documents and the operative guide, concerning these standards, the Consiglio Nazionale Dottori Commercilisti e Esperti Contabili, there is no trace of differentiation between the concept of relevance and materiality. Everything is merged into the term meaningfulness, which includes both ideas, but leaves the precise definition of the boundaries of meaningfulness itself to the interpreter.

Already from these notes, it can be understood how translation into the local language often creates considerable problems in identifying, in a precise manner, the concept of relevance and materiality also because, in reality, these principles show such inter-relationships and correlations as to make it difficult

to contrast the two concepts. As has already been pointed out, materiality is often identified as part of relevance, but, at the same time, the definitions provided show clear overlaps and intersections. For this reason, one may wonder whether it is not time to modify these terms by finding a single concept that encompasses them both. In this way, it would solve any interpretative problems. The following pages will show how this interpretative problem becomes notable in certain circumstances that will address in the following paragraphs.

4) Materiality and relevance in USA experience in Sec regulations , FASB and AIPCA.

In Sec Regulations, Title 17, part 210, Form and content of requirement for financial statement, Application of Regulation S-X, issued in 1933 and continuously updated, it can see that the term relevance is absent. On the other hand, Materiality is present in several paragraphs, and part of the Regulation, as mentioned above, is devoted to this topic.

In § 210.1.02, it is stated :

"(2) Attestation report on internal control over financial reporting. The term attestation report on internal control over financial reporting means a report in which a registered public accounting firm expresses an opinion, either unqualified or adverse, as to whether the registrant maintained, in all material respects, effective internal control over financial reporting, except in the rare circumstance of a scope limitation that cannot be overcome by the registrant or the registered public accounting firm which would result in the accounting firm disclaiming an opinion.

……

(4) Material weakness means a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the registrants annual or interim financial statements will not be prevented or detected on a timely basis

…

(o) Material. The term material, when used to qualify a requirement for the furnishing of information as to any subject, limits the information required to those matters about which an average prudent investor ought reasonably to be informed.".

.

…

§ 210.02.01 Qualifications of Accountants

. (D) The accounting firm, any covered person in the firm, any of his or her immediate family members, or any group of the above persons has any material indirect investment in an audit client. For purposes of this paragraph, the term material

indirect investment does not include ownership by any covered person in the firm, any of his or her immediate family members, or any group of the above persons of 5% or less of the outstanding shares of a diversified management investment company, as defined by section 5(b)(1) of the Investment Company Act of 1940, 15 U.S.C. 80a-5(b)(1), that invests in an audit client.

The above-mentioned document issued by the SEC contains various references to materiality, but their meaningfulness is reduced. For this reason, it is not deemed appropriate to quote these parts in this article.

It is noteworthy that in the SEC, as mentioned above document, only a few items are indicated concerning which percentages can be identified below which the item or error is not material. The items are minimal, but it is interesting to read when contained in the SEC Staff Accounting Bulletin: no. 99 Materiality because, in this document, it is made very explicitly clear that, even where reference is made to a threshold percentage, this alone cannot be considered sufficient to consider an item or error material or non-material. The SEC Staff Accounting Bulletin: no. 99 Materiality states that :

"**Question**: Each Statement of Financial Accounting Standards adopted by the Financial Accounting Standards Board ("FASB") states, "The provisions of this Statement need not be applied to immaterial items." In the staff's view, may a registrant or the auditor of its financial statements assume the immateriality of items that fall below a percentage threshold set by management or the auditor to determine whether amounts and items are material to the financial statements?

Interpretive Response: No. The staff is aware that certain registrants, over time, have developed quantitative thresholds as "rules of thumb" to assist in the preparation of their financial statements, and that auditors also have used these thresholds in their evaluation of whether items might be considered material to users of a registrant's financial statements. One rule of thumb in particular suggests that the misstatement or omission[2] of an item that falls under a 5% threshold is not material in the absence of particularly egregious circumstances, such as self-dealing or misappropriation by senior management. The staff reminds registrants and the auditors of their financial statements that exclusive reliance on this or any percentage or numerical threshold has no basis in the accounting literature or the law.

The use of a percentage as a numerical threshold, such as 5%, may provide the basis for a preliminary assumption that—without considering all relevant circumstances—a deviation of less than the specified percentage with respect to a particular item on the registrant's financial statements is unlikely to be material. The staff has no objection to such a "rule of thumb" as an initial step in assessing materiality. But quantifying, in percentage terms, the magnitude of a misstatement is only the beginning of an analysis of materiality; it cannot appropriately be used as a substitute for a full analysis of all relevant considerations. Materiality concerns the significance of an item to users of a registrant's financial statements. A matter is "material" if there is a substantial likelihood that a reasonable person would consider it important. In its Statement of Financial Accounting Concepts No. 2, the FASB stated the essence of the concept of materiality as follows:

The omission or misstatement of an item in a financial report is material if, in the light of surrounding circumstances, the magnitude of the item is such that it is probable that the judgment of a reasonable person relying upon the report would have been changed or influenced by the inclusion or correction of the item.

This formulation in the accounting literature is in substance identical to the formulation used by the courts in interpreting the federal securities laws. The Supreme Court has held that a fact is material if there is a substantial likelihood that the . . . fact would have been viewed by the reasonable investor as having significantly altered the "total mix" of information made available. [4]

Under the governing principles, an assessment of materiality requires that one views the facts in the context of the "surrounding circumstances," as the accounting literature puts it, or the "total mix" of information, in the words of the Supreme Court. In the context of a misstatement of a financial statement item, while the "total mix" includes the size in numerical or percentage terms of the misstatement, it also includes the factual context in which the user of financial statements would view the financial statement item. The shorthand in the accounting and auditing literature for this analysis is that financial management and the auditor must consider both "quantitative" and "qualitative" factors in assessing an item's materiality.[5] Court decisions, Commission rules and enforcement actions, and accounting and auditing literature[6] have all considered "qualitative" factors in various contexts.

The FASB has long emphasized that materiality cannot be reduced to a numerical formula. In its Concepts Statement No. 2, the FASB noted that some had urged it to promulgate quantitative materiality guides for use in a variety of situations. The FASB rejected such an approach as representing only a "minority view," stating:

The predominant view is that materiality judgments can properly be made only by those who have all the facts. The Board's present position is that no general standards of materiality could be formulated to take into account all the considerations that enter into an experienced human judgment. [7]

The FASB noted that, in certain limited circumstances, the Commission and other authoritative bodies had issued quantitative materiality guidance, citing as examples guidelines ranging from one to ten percent with respect to a variety of disclosures. And it took account of contradictory studies, one showing a lack of uniformity among auditors on materiality judgments, and another suggesting widespread use of a "rule of thumb" of five to ten percent of net income[9] The FASB also considered whether an evaluation of materiality could be based solely on anticipating the market's reaction to accounting information.[10]

The FASB rejected a formulaic approach to discharging "the onerous duty of making materiality decisions"[11] in favor of an approach that takes into account all the relevant considerations. In so doing, it made clear that—

[M]agnitude by itself, without regard to the nature of the item and the circumstances in which the judgment has to be made, will not generally be a sufficient basis for a materiality judgment.[12]

Evaluation of materiality requires a registrant and its auditor to consider *all* the relevant circumstances, and the staff believes that there are numerous circumstances in which misstatements below 5% could well be material. Qualitative factors may cause misstatements of quantitatively small amounts to be material; as stated in the auditing literature:

As a result of the interaction of quantitative and qualitative considerations in materiality judgments, misstatements of relatively small amounts that come to the auditor's attention could have a material effect on the financial statements.

Among the considerations that may well render material a quantitatively small misstatement of a financial statement item are—

- whether the misstatement arises from an item capable of precise measurement or whether it arises from an estimate and, if so, the degree of imprecision inherent in the estimate[14]
- whether the misstatement masks a change in earnings or other trends
- whether the misstatement hides a failure to meet analysts' consensus expectations for the enterprise
- whether the misstatement changes a loss into income or vice versa
- whether the misstatement concerns a segment or other portion of the registrant's business that has been identified as playing a significant role in the registrant's operations or profitability
- whether the misstatement affects the registrant's compliance with regulatory requirements
- whether the misstatement affects the registrant's compliance with loan covenants or other contractual requirements
- whether the misstatement has the effect of increasing management's compensation—for example, by satisfying requirements for the award of bonuses or other forms of incentive compensation
- whether the misstatement involves concealment of an unlawful transaction.

This is not an exhaustive list of the circumstances that may affect the materiality of a quantitatively small misstatement.[15] Among other factors, the demonstrated volatility of the price of a registrant's securities in response to certain types of disclosures may provide guidance as to whether investors regard quantitatively small misstatements as material. Consideration of potential market reaction to disclosure of a misstatement is by itself "too blunt an instrument to be depended on" in considering whether a fact is material.[16] When, however, management or the independent auditor expects (based, for example, on a pattern of market performance) that a known misstatement may result in a significant positive or negative market reaction, that expected reaction should be taken into account when considering whether a misstatement is material.[17]

For the reasons noted above, the staff believes that a registrant and the auditors of its financial statements should not assume that even small intentional misstatements in financial statements, for example those pursuant to actions to "manage" earnings, are immaterial.ile the intent of management does not render a misstatement material, it may provide significant evidence of materiality. The evidence may be particularly compelling where management has intentionally misstated items in the financial statements to "manage" reported earnings. In that instance, it presumably has done so believing that the resulting amounts and trends would be significant to users of the registrant's financial statements The staff believes that investors generally would regard as significant a management practice to over- or

under-state earnings up to an amount just short of a percentage threshold in order to “manage” earnings. Investors presumably also would regard as significant an accounting practice that, in essence, rendered all earnings figures subject to a management-directed margin of misstatement.

The materiality of a misstatement may turn on where it appears in the financial statements. For example, a misstatement may involve a segment of the registrant’s operations. In that instance, in assessing materiality of a misstatement to the financial statements taken as a whole, registrants and their auditors should consider not only the size of the misstatement but also the significance of the segment information to the financial statements taken as a whole.[20] “A misstatement of the revenue and operating profit of a relatively small segment that is represented by management to be important to the future profitability of the entity is more likely to be material to investors than a misstatement in a segment that management has not identified as especially important. In assessing the materiality of misstatements in segment information -as with materiality generally- situations may arise in practice where the auditor will conclude that a matter relating to segment information is qualitatively material even though, in his or her judgment, it is quantitatively immaterial to the financial statements taken as a whole.”

Aggregating and Netting Misstatements

In determining whether multiple misstatements cause the financial statements to be materially misstated, registrants and the auditors of their financial statements should consider each misstatement separately and the aggregate effect of all misstatements. A registrant and its auditor should evaluate misstatements in light of quantitative and qualitative factors and “consider whether, in relation to individual line item amounts, subtotals, or totals in the financial statements, they materially misstate the financial statements taken as a whole.”[24] This requires consideration of -the significance of an item to a particular entity (for example, inventories to a manufacturing company), the pervasiveness of the misstatement (such as whether it affects the presentation of numerous financial statement items), and the effect of the misstatement on the financial statements taken as a whole ....

Registrants and their auditors first should consider whether each misstatement is material, irrespective of its effect when combined with other misstatements. The literature notes that the analysis should consider whether the misstatement of “individual amounts” causes a material misstatement of the financial statements taken as a whole. As with materiality generally, this analysis requires consideration of both quantitative and qualitative factors.

If the misstatement of an individual amount causes the financial statements as a whole to be materially misstated, that effect cannot be eliminated by other misstatements whose effect may be to diminish the impact of the misstatement on other financial statement items. To take an obvious example, if a registrant’s revenues are a material financial statement item and if they are materially overstated, the financial statements taken as a whole will be materially misleading even if the effect on earnings is completely offset by an equivalent overstatement of expenses.

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. Registrants and the auditors of their financial statements accordingly should consider the effect of the misstatement on subtotals or totals. The auditor should aggregate all misstatements that affect each subtotal or total and consider whether the misstatements in the aggregate affect the subtotal or total in a way that causes the registrant's financial statements taken as a whole to be materially misleading.[26]

The staff believes that, in considering the aggregate effect of multiple misstatements on a subtotal or total, registrants and the auditors of their financial statements should exercise particular care when considering whether to offset (or the appropriateness of offsetting) a misstatement of an estimated amount with a misstatement of an item capable of precise measurement. As noted above, assessments of materiality should never be purely mechanical; given the imprecision inherent in estimates, there is by definition a corresponding imprecision in the aggregation of misstatements involving estimates with those that do not involve an estimate.

Registrants and auditors also should consider the effect of misstatements from prior periods on the current financial statements. For example, the auditing literature states,

Matters underlying adjustments proposed by the auditor but not recorded by the entity could potentially cause future financial statements to be materially misstated, even though the auditor has concluded that the adjustments are not material to the current financial statements.[27]

This may be particularly the case where immaterial misstatements recur in several years and the cumulative effect becomes material in the current year.

2. Immaterial Misstatements That are Intentional

Facts: A registrant's management intentionally has made adjustments to various financial statement items in a manner inconsistent with GAAP. In each accounting period in which such actions were taken, none of the individual adjustments is by itself material, nor is the aggregate effect on the financial statements taken as a whole material for the period. The registrant's earnings "management" has been effected at the direction or acquiescence of management in the belief that any deviations from GAAP have been immaterial and that accordingly the accounting is permissible.

Question: In the staff's view, may a registrant make intentional immaterial misstatements in its financial statements?

Interpretive Response: No. In certain circumstances, intentional immaterial misstatements are unlawful.

Considerations of the Books and Records Provisions Under the Exchange Act

Even if misstatements are immaterial, registrants must comply with Sections 13(b)(2)-(7) of the Securities Exchange Act of 1934 (the "Exchange Act"). Under these provisions, each registrant with

securities registered pursuant to Section 12 of the Exchange Act, or required to file reports pursuant to Section 15(d), must make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of assets of the registrant and must maintain internal accounting controls that are sufficient to provide reasonable assurances that, among other things, transactions are recorded as necessary to permit the preparation of financial statements in conformity with GAAP. In this context, determinations of what constitutes "reasonable assurance" and "reasonable detail" are based not on a "materiality" analysis but on the level of detail and degree of assurance that would satisfy prudent officials in the conduct of their own affairs. Accordingly, failure to record accurately immaterial items, in some instances, may result in violations of the securities laws.

The staff recognizes that there is limited authoritative guidance regarding the "reasonableness" standard in Section 13(b)(2) of the Exchange Act. A principal statement of the Commission's policy in this area is set forth in an address given in 1981 by then Chairman Harold M. Williams. In his address, Chairman Williams noted that, like materiality, "reasonableness" is not an "absolute standard of exactitude for corporate records." Unlike materiality, however, "reasonableness" is not solely a measure of the significance of a financial statement item to investors. "Reasonableness," in this context, reflects a judgment as to whether an issuer's failure to correct a known misstatement implicates the purposes underlying the accounting provisions of Sections 13(b)(2)-(7) of the Exchange Act.

In assessing whether a misstatement results in a violation of a registrant's obligation to keep books and records that are accurate "in reasonable detail," registrants and their auditors should consider, in addition to the factors discussed above concerning an evaluation of a misstatement's potential materiality, the factors set forth below.

- **The significance of the misstatement**. Though the staff does not believe that registrants need to make finely calibrated determinations of significance with respect to immaterial items, plainly it is "reasonable" to treat misstatements whose effects are clearly inconsequential differently than more significant ones.
- **How the misstatement arose**. It is unlikely that it is ever "reasonable" for registrants to record misstatements or not to correct known misstatements -even immaterial ones- as part of an ongoing effort directed by or known to senior management for the purposes of "managing" earnings. On the other hand, insignificant misstatements that arise from the operation of systems or recurring processes in the normal course of business generally will not cause a registrant's books to be inaccurate "in reasonable detail."[38]
- **The cost of correcting the misstatement**. The books and records provisions of the Exchange Act do not require registrants to make major expenditures to correct small misstatements.[39] Conversely, where there is little cost or delay involved in correcting a misstatement, failing to do so is unlikely to be "reasonable."
- **The clarity of authoritative accounting guidance with respect to the misstatement**. Where reasonable minds may differ about the appropriate accounting treatment of a financial statement

> item, a failure to correct it may not render the registrant's financial statements inaccurate "in reasonable detail." Where, however, there is little ground for reasonable disagreement, the case for leaving a misstatement uncorrected is correspondingly weaker.

There may be other indicators of "reasonableness" that registrants and their auditors may ordinarily consider. Because the judgment is not mechanical, the staff will be inclined to continue to defer to judgments that "allow a business, acting in good faith, to comply with the Act's accounting provisions in an innovative and cost-effective way."

The Auditor's Response to Intentional Misstatements

Section 10A(b) of the Exchange Act requires auditors to take certain actions upon discovery of an "illegal act."[41] The statute specifies that these obligations are triggered "whether or not [the illegal acts are] perceived to have a material effect on the financial statements of the issuer . . . ." Among other things, Section 10A(b)(1) requires the auditor to inform the appropriate level of management of an illegal act (unless clearly inconsequential) and assure that the registrant's audit committee is "adequately informed" with respect to the illegal act.

As noted, an intentional misstatement of immaterial items in a registrant's financial statements may violate Section 13(b)(2) of the Exchange Act and thus be an illegal act. When such a violation occurs, an auditor must take steps to see that the registrant's audit committee is "adequately informed" about the illegal act. Because Section 10A(b)(1) is triggered regardless of whether an illegal act has a material effect on the registrant's financial statements, where the illegal act consists of a misstatement in the registrant's financial statements, the auditor will be required to report that illegal act to the audit committee irrespective of any "netting" of the misstatements with other financial statement items.

The requirements of Section 10A echo the auditing literature. See, for example, Statement on Auditing Standards No. ("SAS") 54, "Illegal Acts by Clients," and SAS 82, "Consideration of Fraud in a Financial Statement Audit." Pursuant to paragraph 38 of SAS 82, if the auditor determines there is evidence that fraud may exist, the auditor must discuss the matter with the appropriate level of management. The auditor must report directly to the audit committee fraud involving senior management and fraud that causes a material misstatement of the financial statements. Paragraph 4 of SAS 82 states that "misstatements arising from fraudulent financial reporting are intentional misstatements or omissions of amounts or disclosures in financial statements to deceive financial statement users." SAS 82 further states that fraudulent financial reporting may involve falsification or alteration of accounting records; misrepresenting or omitting events, transactions or other information in the financial statements; and the intentional misapplication of accounting principles relating to amounts, classifications, the manner of presentation, or disclosures in the financial statements The clear implication of SAS 82 is that immaterial misstatements may be fraudulent financial reporting.

Auditors that learn of intentional misstatements may also be required to (1) re-evaluate the degree of audit risk involved in the audit engagement, (2) determine whether to revise the nature, timing, and extent of audit procedures accordingly, and (3) consider whether to resign.

Intentional misstatements also may signal the existence of reportable conditions or material weaknesses in the registrant's system of internal accounting control designed to detect and deter improper accounting and financial reporting. As stated by the National Commission on Fraudulent Financial Reporting, also known as the Treadway Commission, in its 1987 report,

The tone set by top management -the corporate environment or culture within which financial reporting occurs- is the most important factor contributing to the integrity of the financial reporting process. Notwithstanding an impressive set of written rules and procedures, if the tone set by management is lax, fraudulent financial reporting is more likely to occur.

An auditor is required to report to a registrant's audit committee any reportable conditions or material weaknesses in a registrant's system of internal accounting control that the auditor discovers in the course of the examination of the registrant's financial statements.

GAAP Precedence Over Industry Practice

Some have argued to the staff that registrants should be permitted to follow an industry accounting practice even though that practice is inconsistent with authoritative accounting literature. This situation might occur if a practice is developed when there are few transactions and the accounting results are clearly inconsequential, and that practice never changes despite a subsequent growth in the number or materiality of such transactions. The staff disagrees with this argument. Authoritative literature takes precedence over industry practice that is contrary to GAAP.

General Comments

This SAB is not intended to change current law or guidance in the accounting or auditing literature. This SAB and the authoritative accounting literature cannot specifically address all of the novel and complex business transactions and events that may occur. Accordingly, registrants may account for, and make disclosures about, these transactions and events based on analogies to similar situations or other factors. The staff may not, however, always be persuaded that a registrant's determination is the most appropriate under the circumstances. When disagreements occur after a transaction or an event has been reported, the consequences may be severe for registrants, auditors, and, most importantly, the users of financial statements who have a right to expect consistent accounting and reporting for, and disclosure of, similar transactions and events. The staff, therefore, encourages registrants and auditors to discuss on a timely basis with the staff proposed accounting treatments for, or disclosures about, transactions or events that are not specifically covered by the existing accounting literature."

Alongside the SEC regulations, one can also mention the principles issued by AIPCA. One can see that the concept of relevance is absent, and only the term materiality is present. The most crucial document

in this regard is the AU principle Section 320 Materiality in Planning and performing an Audit. In December 2019, the AICPA Auditing Standards Board (ASB) issued Statement on Auditing Standards (SAS) No. 138, Amendments to the Description of the Concept of Materiality, and Statement on Standards for Attestation Engagements (SSAE) No. 20 of the same title to respectively amend various AU-C and AT-C sections in AICPA Professional Standards. What has changed? The description of the concept of materiality has changed. The ASB's current description of the concept of materiality is consistent with the definition of materiality used by the International Accounting Standards Board (IASB) and the International Auditing and Assurance Standards Board (IAASB). SAS No. 138 and SSAE No. 20 align the materiality concepts discussed in AICPA Professional Standards with the description of materiality used by the U.S. judicial system, the auditing standards of the Public Company Accounting Oversight Board (PCAOB), the U.S. Securities and Exchange Commission (SEC), and the Financial Accounting Standards Board (FASB). The ASB believes it is in the public interest to eliminate inconsistencies between the AICPA Professional Standards and the description of materiality used by the U.S. judicial system and other U.S. standard setters and regulators. The ASB believes that, because the revised definition is aligned with the FASB, the revised description is substantially consistent with current U.S. firm practices with respect to determining and applying materiality in an audit or attest engagement and, accordingly, the amendments are neither expected nor intended to change U.S. practice. The revised description of materiality is as follows: Misstatements, including omissions, are considered to be material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

After these emendations, AU Section 320 Materiality in Planning and performin an Audit states:

".01 This section addresses the auditor's responsibility to apply the concept of materiality in planning and performing an audit of financial statements. Section 450, Evaluation of Misstatements Identified During the Audit, explains how materiality is applied in evaluating the effect of identified misstatements on the audit and the effect of uncorrected misstatements, if any, on the financial statements. Materiality in the Context of an Audit .

.02 Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and fair presentation of financial statements. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that

• misstatements, including omissions, are considered to be material if they there is a substantial likelihood that, individually or in the aggregate, they could reasonably be expected to would influence the economic decisions of users judgment made by a reasonable user based on the basis of the financial statements.

• judgments about materiality are made in light of surrounding circumstances and are affected by the size or nature of a misstatement, or a combination of both.

• judgments about materiality involve both qualitative and quantitative considerations.

• judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.

.03 Such a discussion about materiality provides a frame of reference to the auditor in determining materiality for the audit. If the applicable financial reporting framework does not include a discussion of the concept of materiality, the characteristics referred to in paragraph .02 provide the auditor with such a frame of reference.

.04 The auditor's determination of materiality is a matter of professional judgment and is affected by the auditor's perception of the financial information needs of users of the financial statements. For purposes of determining materiality, the auditor may assume that reasonable users

a. have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;

b. understand that financial statements are prepared, presented, and audited to levels of materiality;

c. recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment, and the conideration of future events; and

d. make reasonable judgments based on the information in the financial statements.

.05 The concept of materiality is applied by the auditor both in planning and performing the audit; evaluating the effect of identified misstatements on the audit and the effect of uncorrected misstatements, if any, on the financial statements; and in forming the opinion in the auditor's report.

.06 In planning the audit, the auditor makes judgments about misstatements that will be considered material. These judgments provide a basis for a. determining the nature and extent of risk assessment procedures; b. identifying and assessing the risks of material misstatement; and c. determining the nature, timing, and extent of further audit procedures. The materiality determined when planning the audit does not necessarily establish an amount below which uncorrected misstatements, individually or in the aggregate, will always be evaluated as immaterial. The circumstances related to some misstatements may cause the auditor to evaluate them as material even if they are below materiality. It is not practicable to design audit procedures to detect all misstatements that could be material solely because of their nature (that is, qualitative considerations). However, consideration of the nature of potential misstatements in disclosures is relevant to the design of audit procedures to address risks of material misstatement.1 In addition, when evaluating the effect on the financial statements of all uncorrected misstatements, the auditor considers not only the size but also the nature of uncorrected misstatements, and the particular circumstances of their occurrence. [As amended, effective for audits of financial statements for periods ending on or after December 15, 2021, by SAS No. 134.]

…

.09 For purposes of generally accepted auditing standards (GAAS), the following term has the meaning attributed as follows: Performance materiality. The amount or amounts set by the auditor at less than

materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. If applicable, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for paticular classes of transactions, account balances, or disclosures. Performance materiality is to be distinguished from tolerable mistatement.

.10 When establishing the overall audit strategy, the auditor should determine materiality for the financial statements as a whole. If, in the specific circumstances of the entity, one or more particular classes of transactions, account balances, or disclosures exist for which there is a substantial likelihood that misstatements of lesser amounts than materiality for the financial statements as a whole could reasonably be expected to would influence the economic decisions of users, then, taken judgment made by a reasonable user based on the basis of the financial statements, the auditor also should determine the materiality level or levels to be applied to those particular classes of transactions, account balances, or disclosures.

.11 The auditor should determine performance materiality for purposes of assessing the risks of material misstatement and determining the nature, timing, and extent of further audit procedures.

.12 The auditor should revise materiality for the financial statements as a whole (and, if applicable, the materiality level or levels for particular classes of transactions, account balances, or disclosures) in the event of becoming aware of information during the audit that would have caused the auditor to have determined a different amount (or amounts) initially.

.13 If the auditor concludes that a lower materiality than that initially determined for the financial statements as a whole (and, if applicable, materiality level or levels for particular classes of transactions, account balances, or disclosures) is appropriate, the auditor should determine whether it is necessary to revise performance materiality and whether the nature, timing, and extent of the further audit procedures remain appropriate.

…

.A1 Identifying and assessing the risks of material misstatement involves the use of professional judgment to identify those classes of transactions, account balances, and disclosures, including qualitative disclosures, the misstatement of which could be material (in general, misstatements are considered to be material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements). When considering whether misstatements in qualitative disclosures could be material, the auditor may identify relevant factors such as the following:

• The circumstances of the entity for the period (For example, the entity may have undertaken a significant business combination during the period.)

• The applicable financial reporting framework, including changes therein (For example, a new financial reporting standard may require new qualitative disclosures that are significant to the entity.)

• Qualitative disclosures that are important to users of the financial statements because of the nature of an entity (For example, liquidity risk disclosures may be important to users of the financial statements for a financial istitution).

….

.A6 Determining materiality involves the exercise of professional judgment. A percentage is often applied to a chosen benchmark as a starting point in determining materiality for the financial statements as a whole. Factors that may affect the identification of an appropriate benchmark include the following:

• The elements of the financial statements (for example, assets, liabilities, equity, revenue, or expenses)

• Whether items exist on which the attention of the users of the particular entity's financial statements tends to be focused (for example, for the purpose of evaluating financial performance, users may tend to focus on profit, revenue, or net assets)

• The nature of the entity, where the entity is in its life cycle, and the industry and economic environment in which the entity operates

• The entity's ownership structure and the way it is financed (for example, if an entity is financed solely by debt rather than equity, users may put more emphasis on assets, and claims on them, than on the entity's earnings) • The relative volatility of the benchmark.

…

A15 Planning the audit solely to detect individual material misstatements overlooks the fact that the aggregate of individually immaterial misstatements may cause the financial statements to be materially misstated and leaves no margin for possible undetected misstatements. Performance materiality (which, as defined, is one or more amounts) is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements as a whole. Similarly, performance materiality relating to a materiality level determined for a particular class of transactions, account balance, or disclosure is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in that particular class of transactions, account balance, or disclosure exceeds the materiality level for that particular class of transactions, account balance, or disclosure. The determination of performance materiality is not a simple mechanical calculation and involves the exercise of professional judgment. It is affected by the auditor's understanding of the entity, updated during the performance of the risk assessment procedures, and the nature and extent of misstatements identified in previous audits and, thereby, the auditor's expectations regarding misstatements in the current period."

In 2022, AIPCA issued a document entitled "Materiality considerations for attestation engagements involving aspects of subject matters that canno be quantitatitvely measured and in that important document pointed out that :

1. "Materiality considerations affect engagement

planning, engagement performance, and ultimately, the practitioner's report. In an examination engagement, the practitioner expresses an opinion about whether the subject matter is in accordance with (or based on) the criteria, in all material respects; in a review engagement, the practitioner expresses a conclusion about whether the practitioner is aware of any material modifications that should be made to the subject matter for it to be in accordance with the criteria.

2. In an attestation engagement, the attestation standards define a *misstatement* as "the difference between the measurement or evaluation of the subject matter by the responsible party and the proper measurement or evaluation of the subject matter based on the criteria." 4 Misstatements (including omissions) can be intentional or unintentional, qualitative or quantitative. In certain engagements, a misstatement may be referred to as a *deviation, deficiency, exception or instance of noncompliance*. In general, misstatements, including omissions, are considered to be material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by intended users based on the subject matter.

3. Considering materiality when misstatements in certain aspects of the subject matter cannot be quantified is typically more difficult and less straightforward than when misstatements in subject matters can be quantified. In an audit engagement, for example, the subject matter is the historical financial statements or an element thereof. Misstatements in financial statement amounts can be quantified. Generally accepted auditing standards provide guidance on an auditor's evaluation of misstatements in historical financial statements using both quantitative and qualitative factors. When auditing financial statement amounts, many auditors set materiality by choosing a benchmark, such as net income, revenues or net assets, and applying a specific percentage to the benchmark (for example, 5% of net income) selected based on consideration of various factors.

4. Misstatements in disclosures that accompany historical financial statements are not always quantitatively measurable (for example, the nature and extent of disclosures about related parties). Depending on the disclosure, an auditor assessing misstatements in such disclosures may consider primarily qualitative factors.

5. Attestation engagements can be performed on a variety of subject matters, and many aspects of those subject matters cannot be quantitatively measured or evaluated. Subject matters of commonly performed attestation engagements include the following:

• Description of a system and controls of a service organization, when those controls are relevant to user entities' internal control over financial reporting (in a SOC 1® examination)

• Description of a system and controls of a service organization relevant to security, availability, processing integrity, confidentiality or privacy (in a SOC 2® examination)

• Information about sustainability matters, such as economic, environmental, social and governance performance, presented in various ways, such as in a sustainability report, in a schedule or statement of GHG emissions information or as a presentation of one or more sustainability indicators or sustainability metrics (in a review or examination of sustainability information)

• Compliance with the terms of a contract, law or regulation (in a compliance examination).

6. Only certain aspects of those subject matters lend themselves to quantitative measurement or evaluation (for example, percentage of system downtime, metric tons of GHG emissions, number of instances of noncompliance); many other aspects do not (for example, the nature and extent of disclosures about an entity's sustainability efforts, disclosures included in a description of an entity's internal control system or instances of noncompliance). Such subject matters may present challenges for practitioners when considering materiality in these engagements.

7. Because the attestation standards were written to be applicable to a wide variety of subject matters, they do not provide detailed guidance on considering materiality for specific subject matters. This document focuses on the challenges surrounding materiality considerations when aspects of such subject matters cannot be quantified.

8. In both examination and review engagements, the practitioner is required to consider materiality when planning, performing and reporting on the engagement. For an examination engagement, thepractitioner is required to do the following:

• Consider materiality for the subject matter when establishing an overall engagement strategy.

• Reconsider materiality for the subject matter if the practitioner becomes aware of information during the engagement that would have caused the practitioner to have initially determined a different materiality.

• Identify and assess the risks of material misstatement as the basis for designing and performing further procedures whose nature, timing, and extent are responsive to the assessed risks of material misstatement and allow the practitioner to obtain reasonable assurance about whether the subject matter is in accordance with (or based on) the criteria, in all material respects

• Form an opinion about whether the subject matter is in accordance with (or based on) the criteria, in all material respects. When forming that opinion, the practitioner should evaluate.

— the practitioner's conclusion regarding the sufficiency and appropriateness of evidence obtained and

— whether uncorrected misstatements are material, individually or in the aggregate.

For a review engagement, the practitioner is required to consider materiality when doing the following:

• Determining the nature, timing and extent of procedures.

• Forming a conclusion about whether the practitioner is aware of any material modifications that should be made to the subject matter in order for it to be in accordance with (or based on) the criteria. When forming that conclusion, the practitioner should evaluate

— the practitioner's conclusion regarding the sufficiency and appropriateness of the review evidence obtained; and

— whether uncorrected misstatements are material, individually or in the aggregate.

9. A practitioner's professional judgments about materiality are made in light of engagement facts and circumstances, but they are not affected by the level of assurance; that is, for the same intended users,

materiality for an examination engagement is the same as it is for a review engagement because materiality is based on the information needs of intended users and not on the level of assurance."

In the document mentioned above, there are also examples of materiality referring to specific cases we do not deem interesting to report here.

In the USA, particularly relevant is the FASB, whose Conceptual Framework for Financial Reporting Chapter 8, Notes to Financial Statements, containing amendments to the General Framework, has highlighted some interesting considerations. First, it should note that, unlike the US bodies mentioned above, the FASB, in the cited document, refers to both relevance and materiality. The FASB's Framework 2021 states that:

"73. Relevance is a primary qualitative characteristic. To be relevant, information about an item must have feedback value or predictive value (or both) for users and must be timely. 45 Information is relevant if it has the capacity to make a difference in investors', creditors', or other users' decisions. To be recognized, the information conveyed by including an asset, liability, or change therein in the financial statements must be relevant. 74. The relevance of particular information about an item being considered for recognition cannot be determined in isolation. Relevance should be evaluated in the context of the principal objective of financial reporting: providing information that is useful in making rational investment, credit, and similar decisions.46 Relevance should also be evaluated in the context of the full set of financial statements—with consideration of how recognition of a particular item contributes to the aggregate decision usefulness."

The above-mentioned document also states the Highlight. According to this indication la relevance is the information ….. capable of making a difference in user decisions

The FASB Conceptual Framework for Financial Reporting Chapter 3, Qualitative Characteristics of Useful Financial Information 2018 Fundamental Qualitative Characteristics, states:

"QC5. The fundamental qualitative characteristics are relevance and faithful representation. Relevance QC6. Relevant financial information is capable of making a difference in the decisions made by users. Information may be capable of making a difference in a decision even if some users choose not to take advantage of it or already are aware of it from other sources. QC7. Financial information is capable of making a difference in decisions if it has predictive value, confirmatory value, or both. QC8. Financial information has predictive value if it can be used as an input to processes employed by users to predict future outcomes. Financial information need not be a prediction or forecast to have predictive value. Financial information with predictive value is employed by users in making their own predictions. QC9. Financial information has confirmatory value if it provides feedback (confirms or changes) about previous evaluations. QC10. The predictive value and confirmatory value of financial information are interrelated. Information that has predictive value often also has confirmatory value. For example, revenue information for the current year, which can be used as the basis for predicting revenues in future years, also can be compared with revenue predictions for the current year that were made in past years. The results of those comparisons can help a user to correct and improve the processes that were

used to make those previous predictions. Materiality QC11. Relevance and materiality are defined by what influences or makes a difference to an investor or other decision maker; however, the two concepts can be distinguished from each other. Relevance is a general notion about what type of information is useful to investors. Materiality is entity specific. The omission or misstatement of an item in a financial report is material if, in light of surrounding circumstances, the magnitude of the item is such that it is probable that the 3 judgment of a reasonable person relying upon the report would have been changed or influenced by the inclusion or correction of the item. QC11A. A decision not to disclose certain information or recognize an economic phenomenon may be made, for example, because the amounts involved are too small to make a difference to an investor or other decision maker (they are immaterial). However, magnitude by itself, without regard to the nature of the item and the circumstances in which the judgment has to be made, generally is not a sufficient basis for a materiality judgment. QC11B. No general standards of materiality could be formulated to take into account all the considerations that enter into judgments made by an experienced, reasonable provider of financial information. That is because materiality judgments can properly be made only by those that understand the reporting entity's pertinent facts and circumstances. Whenever an authoritative body imposes materiality rules or standards, it is substituting generalized collective judgments for specific individual judgments, and there is no reason to suppose that the collective judgments always are superior"

In the FASB Concepts Statement No. 3, Elements of Financial Statements of Business Enterprises.40 it i salso stated that:

"39 Individual judgments are required to assess materiality. . . . The essence of the materiality concept is clear. The omission or misstatement of an item in a financial report is material if, in the light of surrounding circumstances, the magnitude of the item is such that it is probable that the judgment of a reasonable person relying upon the report would have been changed or influenced by the inclusion or correction of the item" (Concepts Statement 2, par. 132)

With reference to relevance, evidenzia che "D23. The Board's judgments about whether to establish disclosure requirements are based on broad general considerations of relevance rather than on entityspecific judgments about materiality. Ideally, disclosure requirements would be made applicable only to the specific entities to which they are most important. However, disclosures should have the potential to apply to a broad range of entities (or to a broad range of entities within an identified subset of entities). For example, disclosures may be relevant to a broad range of not-for-profit entities while not being relevant to for profit entities, although that range may not stay constant. While disclosures have relevance to a broad range of entities, they may not be material to all entities to which they may apply. Materiality decisions must be made by each individual entity. As such, the Board should establish requirements that are not so prescriptive that they preclude reporting entities from making materiality judgments". Come si può notare, il FAsb spiega la relevance facendo riferimento, in realtà, alla materiality.

The document emphasises how “relevance and materiality are defined by what influences or makes a difference to an investor or other decision maker; however, the two 32 concepts can be distinguished from each other. Relevance is a general notion about what type of information is useful to investors. Materiality is entity specific”. Anche in questo caso quindi, il concetto di relevance comprende, in sostanza, la materiality.

With regard to materiality, it should be noted that:

“Information to Be Considered for Disclosure

a. Enough information (normally qualitative instead of quantitative) about the phenomenon or phenomena so that a user may access reference materials or other sources of information to understand the phenomenon or phenomena

b. If a user could not reasonably be expected to find adequate information from other sources, an explanation of the nature of the phenomenon or phenomena in enough detail to provide an understanding of how the item might affect prospects for cash flows.”

E’ da notare che anche the Board of the FASB does not have specific materiality thresholds defined.

5) Materiality and relevance in Italian jurisprudence.

As noted in the previous pages, in the Italian OIC accounting standards, materiality does not appear, but only the concept of relevance is referred. In the ISA Italia IFAC auditing standards, the two ideas do not appear; instead, a term is used whose translation could be meaningful.

It is well known that financial reporting if prepared without compliance with the law of the civil code (for unlisted companies) and the national accounting standards OIC, is invalid and can therefore be rendered void by the court. At this point, it is essential to understand the position of the judiciary concerning this issue because the judge is a necessary step if a shareholder or third party considers the resolution approving the financial report to be invalid due to a lack of compliance with the financial reporting postulates of truthfulness, fairness and understandability. These postulates indirectly relate to the principle of relevance and materiality, regardless of the exact translation of the two terms that accounting bodies have decided to adopt.

Lolli, an authoritative Italian author who has addressed this issue, emphasises that “errors in financial reporting that do not affect either the net asset balance or the income achieved during the financial year, only render it useless as an (informative) tool if they are of such a magnitude as to significantly alter the qualitative perception of the asset, income and financial situation contained in the financial statements. Certainly, to assume that errors and misrepresentations ...undermine the informative function of the financial report only if they exceed a certain quantitative threshold is tantamount to introducing an element of legal uncertainty that manifests itself in the greater discretion of the adjudicating body ...This consideration does not, however, lead to the conclusion that only quantitatively significant errors and information gaps are capable of rendering the resolution approving the financial statements null and void. The general clause of true and fair representation necessarily

entails an increase in the judging body's discretion...To verify the legal consequences, the assessment of the influence of each error committed on the representation of the company's situation is an expression of this increased discretion" (Lolli, 2005).

The Italian judiciary also shows acceptance of this principle. In fact, in numerous judgments, one reads that there is no nullity when the violation "is in substance irrelevant because it is devoid of real consistency, merely formal, of immediate perception or easy correction through the information taken in the assembly" (Turin Court of Appeal, 24 August 2000).

In principle, therefore, it can say that the courts agree with "the assertion that violation of the provisions relating to how financial reporting is to be prepared (in this case, Art. 2424, old text) renders the resolution of approval null and void when the general interests protected by the rule are concretely prejudiced, and not also when the impact on them is insignificant or negligible...... It concerns the hypotheses in which the violation is irrelevant because it lacks real consistency, merely formal, of immediate perception or easy correction through the information provided in the meeting. This can be the case either because of the principle of clarity or because of the principle of truth, it therefore prescinds from any form of subordination of the former to the latter and always presupposes an appreciation of fact, referred to the judge of merit, on the substantial insubstantiality or irrelevance of the violation" (Court of Cassation 27 February 2000 no. 27).

Therefore, even the civil judiciary points out that it accepts the principle that an error or missing non-material element cannot invalidate the entire balance sheet. ""In corporate matters, ...the hypotheses of radical nullity of resolutions are limited to situations in which a contrast emerges between such resolutions and rules dictated to protect the general interest that transcends that of the individual shareholder or shareholders and that are directed to prevent a decision from the essential economic-practical purpose of the contract and the company relationship. It is thus explained that when in connection with the resolution of the balance sheet . . are alleged to have infringed the principle of clarity and precision of the financial statements, nullity may well be assumed if the facts alleged to be contrary to that principle prove capable of creating uncertainty or erroneous convictions as to the economic and financial situation for all concerned, in such a way as to result in actual prejudice to the general interest in the truthfulness of the financial statements, the truthfulness and clarity of which is intended to protect not only the individual shareholder(s) but also all third parties and creditors in particular' (Court of Cassation, 22 January 2002, no. 928). 928).

The concept of relevance and materiality, or meaningfulness, is translated by the term tenuity of the fact. This happens above all in the criminal field. In this field, the principle of relevance and material or meaningfulness takes on particular relevance. In this regard, it should be recalled how the Italian criminal code, in Article 131 bis, states that:

"Art. 131-bis.

Exclusion of punishability due to the particular tenuousness of the act

In offences for which a term of imprisonment not exceeding a maximum of five years is provided for, or a fine, alone or jointly with the penalty described above, punishability shall be excluded when, due to the modalities of the conduct and to the slightness of the damage or danger, assessed according to Article 133, first paragraph, the offence is particularly trivial, and the behaviour is not habitual.

The offence may not be considered of particular tenuousness, within the meaning of the first paragraph, when the offender has acted with abject or futile motives, or with cruelty, including to animals, or has used brutality, or has taken advantage of the victim's condition of reduced defence, also concerning the victim's age, or when the conduct has caused or resulted in the death or severe injury of a person as an unintended consequence. The offence may also not be deemed to be of particular tenuousness when prosecuting offences punishable by a maximum term of imprisonment of more than two years and six months, committed on the occasion of or because of sporting events, or in the cases referred to in Articles 336, 337 and 341-bis, when the offence is committed against a public security officer or agent or a judicial police officer or agent in the exercise of their functions, and in the case referred to in Article 343.

The conduct is habitual if the perpetrator has been declared a habitual, professional or trendy delinquent or has committed several offences of the same nature, even if each fact, considered separately, is of particular tenuousness, as well as in the case of offences involving multiple, habitual and repeated conduct.

To determine the term of imprisonment provided for in the first paragraph, no account shall be taken of the circumstances, except for those for which the law establishes a penalty of a type different from the ordinary penalty for the offence and those with special effect. In the latter case, for the application of the first paragraph, the balancing of circumstances referred to in Article 69 shall not be taken into account.

The provision of para. One shall also apply where the law provides for the particular tenuousness of the damage or danger as a mitigating circumstance."

Article 133 of the Criminal Code further states that: "**Severity of the offence: assessment for sentencing purposes**

In exercising the discretionary power indicated in the preceding Article, the judge shall take into account the seriousness of the offence, inferred from

1. from the nature, kind, means, object, time, place and any other modality of the action;
2. the seriousness of the damage or danger caused to the person injured by the offence
3. the intensity of the intent or the degree of guilt.

The judge must also take into account the offender's capacity to commit offences, deduced

1. from the offender's motives for offending and character
2. from the offender's criminal and judicial record and, in general, from his conduct and life prior to the offence
3. from the conduct contemporaneous with or subsequent to the offence
4. the individual, family and social life conditions of the offender."

As can be understood, the tenuousness of the fact or the concept of material also assumes importance in the criminal field and also with reference to accounting or tax issues. With regard to evasion of value-added tax, we may recall when the Court of Cassation ruled on 1 June 2022 with sentence no. 21258: “It is worth mentioning, in this regard, the recent ruling of legitimacy in which, in relation to a concrete case in which the omission exceeding the threshold was equal to approximately 4% of the amount of the latter, the principle was affirmed that “On the subject of failure to pay VAT, the cause of non-punishability provided for by Article 131-bis of the Criminal Code, is applicable where the omission concerned an amount slightly higher than the threshold of punishability, set at €250,000.00 by Article 10-ter of Legislative Decree No. 74 of 2000, by reason of the fact that the degree of offensiveness underlying the offence was assessed by the legislature in determining the threshold of criminal relevance (so also Court of Cassation Sez. 3, no. 12906 of 13.11.2018) It is considered, however, that, for the purposes of the applicability of the aforementioned exemption, the factual datum of the modest exceeding of the punishability threshold assumes relevance only in the presence of the further conditions indicated by Article 131-bis of the Criminal Code and therefore, first and foremost, of the overall lack of seriousness of the conduct”.

Similarly, the Criminal Court of Cassation, in its judgment 12906 of 25 March 2019, held that “it should then be recalled that, as stated by the case law of this Court, on the subject of failure to pay VAT, the cause of non-punishability of the ‘particular tenuousness of the act’, provided for by Article 131-bis of the Criminal Code, is applicable only to the omission for an amount very close to the threshold of punishability, set at €250,000.00 by Article 10-ter of Legislative Decree No. 74 of 2000, in consideration of the fact that the degree of offensiveness giving rise to the offence has already been assessed by the legislature in determining the threshold of criminal relevance.”

This principle had already been emphasised by the Criminal Court of Cassation on 12 October 2012, judgement no. 40774, which held that “... the cause of non-punishability may be deemed to exist only in the presence of the twofold requirement of the particular tenuousness of the offence and of the non-recurrence of the conduct, the particular tenuousness of the offence having to be inferred from the manner of the conduct and from the slightness of the damage or danger, to be assessed on the basis of the criteria indicated by Article 133 of the Criminal Code, i.e.: nature, kind, means, object, time, place and any other modality of the action, seriousness of the damage or danger caused to the person offended by the offence, intensity of the intent or degree of guilt’.

Based on the above, it can be understood how the concepts of relevance, materiality and meaningfulness are important not only in the field of financial reporting but also in the field of jurisprudence concerning criminal offences related to tax evasion or accounting. However, it should be noted that, unlike concerning financial reporting, in Italy, in criminal law, relevance, materiality and meaningfulness can only lead to a reduction in sentence due to the tenuousness of the act if the overall conduct of the subject proves the correctness of this reduction. The Criminal Court of Cassation, in its judgment No 15449 of 15 April 2015, pointed out that ‘compliance with the penalty limits is, however, only the first of the

conditions for the exclusion of punishability, which requires (jointly and not alternatively, as can be inferred from the literal tenor of the provision) the particular tenuousness of the offence and the non-regularity of the conduct.

The first of the 'index-criteria' (as defined in the report attached to the legislative decree scheme) just indicated (particular tenuousness of the offence) is, in turn, divided into two 'index-requirements' (again as defined in the report), which are the manner of the conduct and the slightness of the damage or danger, to be assessed based on the criteria indicated in Article 133 of the Criminal Code, (nature, species, means, object, time, place and any other modality of the action, seriousness of the damage or danger caused to the person offended by the offence, intensity of the intent or degree of guilt).

The judge is therefore required to determine whether, based on the two 'index-requirements' of the manner of the conduct and the slightness of the damage and danger assessed following the guiding criteria set out in paragraph 1 of Article 133 of the criminal code, the 'criterion-indicator' of the particular tenuousness of the offence exists and, with this, that of the non-regularity of the conduct. Only in this case can the fact be considered of specific tenuity and consequently exclude its punishability'.

This position, which refers to Article 133 of the criminal code, has been reaffirmed in all subsequent judgments of the Court of Cassation.

7) Conclusioni

From what we have written in the preceding pages, it can understand how the principles of relevance and materiality identify two fundamental concepts to prepare accurate and informative financial reporting for third parties outside the company. However, the principles of relevance and materiality are not as straightforward to interpret as a superficial reading of these terms might suggest. This is demonstrated by the fact that at the international level, if one compares the principles applied in the USA, in Italy and at the international level through the IAS/IFRS principles, one can see diversified positions and concepts that, if at first reading they may seem the same, at a more careful reading they highlight differences even if, often, these differences are interpretative nuances. However, the problematic nature of the issue is proven, for example, by the fact that in Italy, the national accounting standards issued by the Italian accounting organisation do not include the concepts of relevance and materiality but only relevance. This circumstance shows how this concept, in Italy, indirectly encompasses both relevance and materiality found in the laws and regulations of other countries. One might ask oneself whether, in the face of these differences in terms and substance, it would not be opportune to make an overall intervention so that each country could be based on a single internationally accepted concept. So far, this has not yet happened, even though many passages indicate an attempt to approximate the accounting standards issued by the various bodies responsible for this in the multiple nations. What is interesting to note is that in Italy, for example, these concepts, albeit identified by other verbal terms, transcend financial reporting to enter the criminal field in the broadest sense and, therefore, concerning the issue of evasion and accounting. The writer would like to see a

global approximation of the terms used in the various countries so that shortly, principles can assume that even at the terminological level, identify the same concept with the exact words. Therefore, an integration of the various regulations and concepts is desirable, also concerning the issue of relevance and materiality, until a single term has arrived at that encompasses the two images and is uniformly used by all countries to avoid differentiation in terminology and substance that may lead to interpretation problems when pragmatically assessing whether a term or a financial reporting item is relevance or non-relevance and material or non-material.

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Note

To facilitate reading, I have decided not to include in the text, except in exceptional cases, the names of the scholars who have dealt with the subject under analysis since the bibliography is endless, I have opted not to indicate all the terms of the scholars in the text because this would have meant a continuous interruption of the reading of the complete sentence in which I express my thought