Positive accounting theory essay sample

a) The bank unveiled a plan to tackle community concerns so that it would be seen in a more positive light. Because banks offer services which are so essential (providing an opportunity to exploit customers), they deal with high levels of customers and generally make large profits. Also, interest rates naturally fluctuate between high and low levels (controlled by the government to manage inflation – not the individual banks). For these reasons they have developed a generally bad reputation with the public (exacerbated by Credit Union advertisements etc). By making this voluntary disclosure to the public, ANZ is trying to “ win over” customers by showing their concerns for the community. This is an example of Positive Accounting Theory (PAT) – a theory which attempts to explain and predict how groups in an organisation (eg. management, owners, creditors; stakeholders) will interact with one another. In this case, ANZ has made a voluntary social disclosure to the public (ie. its customers) in order to “ soften the blow” of the political costs which are often imposed on banks.

b)

Because the majority of the voting public are also customers of one of the big four banks in Australia (Commonwealth, NAB, ANZ & Westpac), external political costs are often imposed on the banking industry. Because banks make such large profits, they are seen as “ villains” by the public – providing a big target for politicians to aim at. PAT predicts that governments will act in a way to please the voting public so that they will stay in power. This article draws particular reference to the fact that it is an “ election year” – this means that politicians make particular efforts to make sure that they are seen as bringing the “ big bad banks” into line.

c)

Yes, I believe that community concern would not be as great if the bank was not so profitable. Because banks are so profitable, customers (many with mortgages, loans etc that are a major financial burden in their lives) wonder why the banks don't pass more of these profits onto them by reducing fees or interest rates (many customers don't understand the economic ramifications of banks changing interest rates & blame the banks for high interest rates). If banks were not so profitable, then they would have a legitimate reason (in the eyes of customers) for not reducing fees to ease the burden on customers. However, the banks would argue that their main priority is the shareholders – therefore they must act in a way which pleases them ie. by maximising profits.

d)

Yes, it is possible that community concerns about profits made by the banks might motivate the banks to adopt accounting policies that reduce their reported profits. The political cost hypothesis of PAT states that firms subject to political scrutiny will adopt accounting methods that reduce reported income. However, the banks cannot provide one set of reports to the community and another to investors. It is my belief that because the main priority of banks are the shareholders, banks will try and report as high a profit figure as possible to encourage investors and drive up the share price. If one of the banks lags behind the others in terms of profit, they will lose shareholders as they act to get the best possible return on their investment.

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a)

A masthead would be classified as an intangible asset as it is a non-monetary asset without physical substance. Under the new accounting standard (adopted from international accounting standards) AASB 138 " Intangible Assets", internally generated intangible assets cannot be recognised in the balance sheet, whether they are identifiable or not. The company has developed the masthead, therefore it cannot be classified as an asset in the balance sheet (and therefore it can't be revalued). However, if the company was to be purchased, a knowledgeable buyer would factor the masthead's value into consideration. The buyer would be able to recognise the purchased masthead in their balance sheet as an intangible asset (at cost).

b)

A publishing title is a separable intangible asset. Because the company has purchased the publishing title from an external party it can be recognised in the balance sheet at cost ($1. 2 million). If there is an active market for this asset then it may be revalued to its fair value. It is likely that there would be an active market for a very successful book (management has already estimated that they could receive around $1. 5 million if they " put it on the market"). Also the company purchased the publishing title as a separate asset when another company went into liquidation. Because the seller was being liquidated, it is likely that the publishing title was undervalued when sold; therefore a revaluation to fair value would be necessary.

DR – Publishing Title $300, 000

CR – Revaluation Reserve $300, 000

c)

A franchise as a separable intangible asset (ie. the license to operate a franchise). The company purchased the franchise for $100, 000. There is an active market for this asset. There is even a current market price for this asset ($200, 000). Therefore this asset can be revalued to fair value.

DR – Franchise $100, 000

CR – Revaluation Reserve$100, 000

d)

Under AASB 138 development expenditure can be deferred when the following criterion is met:

– The project is likely to proceed & lead to a saleable or usable asset.

– Development expenditure can be measured reliably.

– It is probable that future economic benefits will result.

The company already has deferred development costs of $520, 000. Therefore it can be assumed (if the accountants are doing their jobs properly) that the development meets the criteria. However, this amount can only be carried forward; it cannot be revalued to its “ estimated recoverable amount”. Some of the money spent to generate the estimated recoverable amount of the project of $860, 000 would have already been expensed in the research phase, when it was unknown if future economic benefits would occur (or even be probable).