

# Fast codification essay sample



**ASSIGN  
BUSTER**

The essential characteristics of accounting are

- (1) The identification, measurement, and communication of financial information about
- (2) Economic entities to
- (3) Interested parties.

Financial accounting is the process that culminates in the preparation of financial reports on the enterprise for use by both internal and external parties. Users of these financial reports include investors, creditors, managers, unions, and government agencies.

Managerial accounting is the process of identifying, measuring, analyzing, and communicating financial information needed by management to plan, control, and evaluates a company's operations.

The financial statements most frequently provided are:

- (1) The balance sheet,
- (2) The income statement,
- (3) The statement of cash flows, and
- (4) The statement of owners' or stockholders' equity.

Capital Allocation Process:

Financial Reporting- The financial information a company provides to help users with capital allocation decisions about the company Users (present and potential- Investors and creditors use financial reports to make their capital allocation decisions Capital Allocation -The process of determining how and at what cost money is allocated among competing interests.

The objective of general-purpose financial reporting is to provide financial information about the reporting entity that is useful to present and potential equity investors, lenders, and other creditors in decisions about providing resources to the entity.

General-purpose financial statements provide financial reporting information to a wide variety of users

Entity Perspective- As part of the objective of general-purpose financial reporting, an entity perspective is adopted. Companies are viewed as separate and distinct from their owners (present Shareholders) using this perspective.

A perspective that financial reporting should be focused only on the needs of shareholders—often referred to as the proprietary perspective—is not considered appropriate.

Decision-Usefulness – Investors are interested in financial reporting because it provides information that is useful for making decisions (referred to as the decision-usefulness approach).

The objective of accrual-basis accounting: It ensures that a company records events that change its financial statements in the periods in which the events occur, rather than only in the periods in which it receives or pays cash.

General purpose financial statements. Are expected to present fairly, clearly, and completely the company's financial operations.

## PARTIES INVOLVED IN STANDARD-SETTING

Three organizations are instrumental in the development of financial accounting standards (GAAP) in the United States:

1. Securities and Exchange Commission (SEC)
2. American Institute of Certified Public Accountants (AICPA)
3. Financial Accounting Standards Board (FASB)

The federal government established the Securities and Exchange Commission (SEC) to help develop and standardize financial information presented to stockholders. The SEC is a federal agency and relies on the FASB to develop accounting standard.

The American Institute of Certified Public Accountants (AICPA), which is the national professional organization of practicing Certified Public Accountants (CPAs), has been an important contributor to the development of GAAP.

The Committee on Accounting Procedure (CAP), composed of practicing CPAs, issued 51 Accounting Research Bulletins during the years 1939 to 1959. These bulletins dealt with a variety of accounting problems.

The major purposes of the Accounting Principles Board (APB) were to: (1) Advance the written expression of accounting principles, (2) Determine appropriate practices, and (3) Narrow the areas of difference and inconsistency in practice

The Board's official pronouncements, called APB Opinions, were intended to be based mainly on research studies and be supported by reason and analysis.

The FASAC consults with the FASB on major policy and technical issues and also helps select task force members.

### Due Process

In establishing financial accounting standards, the FASB relies on two basic premises: (1) The FASB should be responsive to the needs and viewpoints of the entire economic community, not just the public accounting profession. (2) It should operate in full view of the public through a “ due process” system that gives interested persons ample opportunity to make their views known.

### The Due Process System of the FASB

- \* Topics identified and placed on Board’s agenda.
- \* Research and analysis conducted and preliminary views of pros and cons issued. \* Public hearing on proposed standard
- \* Board evaluates research and public response and issues exposure draft. \* Board evaluates responses and changes exposure draft, if necessary. Final standard issued. Public hearing on proposed

### Types of Pronouncements

The FASB issues three major types of pronouncements:

1. Standards, Interpretations, and Staff Positions.
2. Financial Accounting Concepts.
3. Emerging Issues Task Force Statements

Standards, Interpretations, and Staff Positions. Financial accounting standards issued by the FASB are considered generally accepted accounting principles. In addition, the FASB has also issued interpretations that modify

or extend existing standards. Finally, the FASB issues staff positions, which provide interpretive guidance and also minor amendments to standards and interpretations

Emerging Issues Task Force (EITF). The EITF is comprised of representatives from CPA firms and financial statement preparers. The purpose of the task force is to reach a consensus on how to account for new and unusual financial transactions that may potentially create differing financial reporting practices. Examples include accounting for pension plan terminations, revenue from barter transactions by Internet companies, and excessive amounts paid to takeover specialists

What is GAAP? The major sources of GAAP come from the organizations discussed Earlier in this chapter. It is composed of a mixture of over 2, 000 documents that have developed over the last 60 years or so.

GAAP Documents

AICPA Accounting Interpretations

FASB Emerging Issues Task Force

FASB Technical Bulletins AICPA Statements of Position

APB Opinions

AICPA AcSEC Practice Bulletins

FASB Implementation Guides (Q and A)

Widely recognized and prevalent industry practices

AICPA Industry Audit and Accounting Guides

FASB Standards, Interpretations, and Staff Positions

AICPA Accounting Research Bulletins:

Topic- Provides a collection of related guidance on a given subject, such as receivables or leases. Subtopics-Subset of a topic and distinguished by type or scope. For example, overall and troubled-debt restructurings are two subtopics of receivables Paragraphs- This level is where you will find the substantive content related to the issue researched. (All other levels exist essentially to find the material related to the paragraph level content.) Sections Indicate the type of content in a subtopic, such as initial measurement. In some cases, subsections are used but not numbered.

#### User Groups that Influence the Formulation of Accounting Standards

- \* Financial community-(analysts, bankers, etc.)
- \* Government -(SEC, IRS, other agencies)
- \* Industry associations-CPAs and
- \* accounting firms-AICPA (AcSEC)
- \* Academicians
- \* Investing public
- \* Business entities
- \* Preparers-(e. g., Financial Executives

the Sarbanes-Oxley Act introduces sweeping changes to the institutional structure of the accounting profession. The following are some of the key provisions of the legislation. • Establishes an oversight board, the Public Company Accounting Oversight Board (PCAOB), for accounting practices. The PCAOB has oversight and enforcement authority and establishes auditing, quality control, and independence standards and rules. • Implements stronger independence rules for auditors. Audit partners, for example, are required to rotate every five years, and auditors are prohibited from offering

certain types of consulting services to corporate clients. • Requires CEOs and CFOs to personally certify that financial statements and disclosures are accurate and complete, and requires CEOs and CFOs to forfeit bonuses and profits when there is an accounting restatement. • Requires audit committees to be comprised of independent members and members with financial expertise. • Requires codes of ethics for senior financial officers

Some of the challenges facing financial reporting

\* Nonfinancial measurements. Financial reports failed to provide some key performance measures widely used by management, such as customer satisfaction indexes, backlog information, and reject rates on goods purchased. \* Forward-looking information. Financial reports failed to provide forward-looking information needed by present and potential investors and creditors. One individual noted that financial statements in 2012 should have started with the phrase, “ Once upon a time,” to signify their use of historical cost and accumulation of past events. \* Soft assets.

Financial reports focused on hard assets (inventory, plant assets) but failed to provide much information about a company’s soft assets (intangibles). The best assets are often intangible. Consider Microsoft’s know-how and market dominance, Wal-Mart’s expertise in supply chain management, and Proctor & Gamble’s brand image. \* Timeliness. Companies only prepared financial statements quarterly and provided audited financials annually. Little to no real-time financial statement information was available. \* SUMMARY OF LEARNING OBJECTIVES



Identify the major financial statements and other means of financial reporting. Companies most frequently provide (1) the balance sheet, (2) the income statement, (3) the statement of cash flows, and (4) the statement of owners' or stockholders' equity. Financial reporting other than financial statements may take various forms. Examples include the president's letter and supplementary schedules in the corporate annual report, prospectuses, reports filed with government agencies, news releases, management's forecasts, and descriptions of a company's social or environmental impact.

2 Explain how accounting assists in the efficient use of scarce resources. Accounting provides reliable, relevant, and timely information to managers, investors, and creditors to allow resource allocation to the most efficient enterprises. Accounting also provides measurements of efficiency (profitability) and financial soundness.

3 Identify the objective of financial reporting. The objective of general-purpose financial reporting is to provide financial information about the reporting entity that is useful to present and potential equity investors, lenders, and other creditors in decisions about providing resources to the entity through equity investments and loans or other forms of credit. Information that is decision-useful to investors may also be helpful to other users of financial reporting who are not investors.

4 Explain the need for accounting standards. The accounting profession has attempted to develop a set of standards that is generally accepted and universally practiced. Without this set of standards, each company would have to develop its own standards. Readers of financial statements would

have to familiarize themselves with every company's peculiar accounting and reporting practices. As a result, it would be almost impossible to prepare statements that could be compared.

5 Identify the major policy-setting bodies and their role in the standard-setting process. The Securities and Exchange Commission (SEC) is a federal agency that has the broad powers to prescribe, in whatever detail it desires, the accounting standards to be employed by companies that fall within its jurisdiction. The American Institute of Certified Public Accountants (AICPA) issued standards through its Committee on Accounting Procedure and Accounting Principles Board. The Financial Accounting Standards Board (FASB) establishes and improves standards of financial accounting and reporting for the guidance and education of the public.

6 Explain the meaning of generally accepted accounting principles (GAAP) and the role of the Codification for GAAP. Generally accepted accounting principles (GAAP) are those principles that have substantial authoritative support, such as FASB standards, interpretations, and staff positions, APB Opinions and interpretations, AICPA Accounting Research Bulletins, and other authoritative pronouncements. All these documents and others are now classified in one document referred to as the Codification. The purpose of the Codification is to simplify user access to all authoritative U. S. GAAP. The Codification changes the way GAAP is documented, presented, and updated.

7 Describe the impact of user groups on the rule-making process. User groups may want particular economic events accounted for or reported in a particular way, and they fight hard to get what they want. They especially

target the FASB to influence changes in existing GAAP and in the development of new rules. Because of the accelerated rate of change and the increased complexity of our economy, these pressures have been multiplying. GAAP is as much a product of political action as it is of careful logic or empirical findings. The IASB is working with the FASB toward international convergence of GAAP.

8 Describe some of the challenges facing financial reporting. Financial reports fail to provide (1) some key performance measures widely used by management, (2) forward-looking information needed by investors and creditors, (3) sufficient information on a company's soft assets (intangibles), and (4) real-time financial information.

9 Understand issues related to ethics and financial accounting. Financial accountants are called on for moral discernment and ethical decision-making. Decisions sometimes are difficult because a public consensus has not emerged to formulate a comprehensive ethical system that provides guidelines in making ethical judgments.

#### IFRS SELF-TEST QUESTIONS

1. IFRS stands for: International Financial Reporting Standards. .
2. The major key players on the international side are the: IASB and IOSCO.
3. IFRS is comprised of: International Financial Reporting Standards, International Accounting Standards, and international accounting interpretations
4. The authoritative status of the Framework for the Preparation and

Presentation of Financial Statements is as follows: It is used when there is no standard or interpretation related to the reporting issues under consideration

5. Which of the following statements is true? The IASB structure is quite similar to the FASB's, except the IASB has a larger number of board members.

#### CA1-1 (FASB and Standard-Setting)

Presented below are four statements which you are to identify as true or false. If false, explain why the statement is false.

1. GAAP is the term used to indicate the whole body of FASB authoritative literature. 2. Any company claiming compliance with GAAP must comply with most standards and interpretations but does not have to follow the disclosure requirements.

3. The primary governmental body that has influence over the FASB is the SEC.

4. The FASB has a government mandate and therefore does not have to follow due process in issuing a standard.

CA1-2 (GAAP and Standard-Setting) Presented below are four statements which you are to identify as true or false. If false, explain why the statement is false. 1. The objective of financial statements emphasizes a stewardship approach for reporting financial information. 2. The purpose of the objective of financial reporting is to prepare a balance sheet, an income statement, a statement of cash flows, and a statement of owners' or stockholders' equity. 3. Because they are generally shorter, FASB interpretations are subject to less due process, compared to FASB standards.

4. The objective of financial reporting uses an entity rather than a proprietary approach in determining what information to report.

CA1-3 (Financial Reporting and Accounting Standards) Answer the following multiple-choice questions. 1. GAAP stands for: generally accepted accounting principles

2. Accounting standard-setters use the following process in establishing accounting standards: (a) Research, exposure draft, discussion paper, standard.

(b) Discussion paper, research, exposure draft, standard.

(c) Research, preliminary views, discussion paper, standard.

(d) Research, discussion paper, exposure draft, standard.

3. GAAP is comprised of:

(a) FASB standards, interpretations, and concepts statements. (b) FASB financial standards.

(c) FASB standards, interpretations, EITF consensuses, and accounting rules issued by FASB predecessor organizations.

(d) any accounting guidance included in the FASB Codification.

4. The authoritative status of the conceptual framework is as follows. (a) It is used when there is no standard or interpretation related to the reporting issues under consideration.

(b) It is not as authoritative as a standard but takes precedence over any interpretation related to the reporting issue.

(c) It takes precedence over all other authoritative literature. (d) It has no authoritative status.

5. The objective of financial reporting places most emphasis on: (a) reporting to capital providers.

(b) reporting on stewardship.

(c) providing specific guidance related to specific needs.

(d) providing information to individuals who are experts in the field.

6. General-purpose financial statements are prepared primarily for: (a) internal users.

(b) external users.

(c) auditors.

(d) government regulators.

7. Economic consequences of accounting standard-setting means: (a)

standard-setters must give first priority to ensuring that companies do not suffer any adverse effect as a result of a new standard.

(b) standard-setters must ensure that no new costs are incurred when a new standard is issued. (c) the objective of financial reporting should be politically motivated to ensure acceptance by the general public.

(d) accounting standards can have detrimental impacts on the wealth levels of the providers of financial information.

8. The expectations gap is:

(a) what financial information management provides and what users want.

(b) what the public thinks accountants should do and what accountants think they can do. (c) what the governmental agencies want from standard-setting and what the standard-setters provide.

(d) what the users of financial statements want from the government and what is provided.

CA1-4 (Financial Accounting) Omar Morena has recently completed his first year of studying accounting. His instructor for next semester has indicated that the primary focus will be the area of financial accounting. Instructions

- (a) Differentiate between financial accounting and managerial accounting.
- (b) One part of financial accounting involves the preparation of financial statements. What are the financial statements most frequently provided? (c) What is the difference between financial statements and financial reporting?

CA1-5 (Objective of Financial Reporting) Karen Sepan, a recent graduate of the local state university, is presently employed by a large manufacturing company. She has been asked by Jose Martinez, controller, to prepare the company's response to a current Preliminary Views published by the Financial Accounting Standards Board (FASB). Sepan knows that the FASB has a conceptual framework, and she believes that these concept statements could be used to support the company's response to the Preliminary Views. She has prepared a rough draft of the response citing the objective of financial reporting. Instructions

- (a) Identify the objective of financial reporting.
- (b) Describe the level of sophistication expected of the users of financial information by the objective of financial reporting.

Concepts for Analysis 25

26 Chapter 1 Financial Accounting and Accounting Standards

CA1-6 (Accounting Numbers and the Environment) Hardly a day goes by

<https://assignbuster.com/fasb-codification-essay-sample/>

without an article appearing on the crises affecting many of our financial institutions in the United States. It is estimated that the savings and loan (S&L) debacle of the 1980s, for example, ended up costing \$500 billion (\$2,000 for every man, woman, and child in the United States). Some argue that if the S&Ls had been required to report their investments at fair value instead of cost, large losses would have been reported earlier, which would have signaled regulators to close those S&Ls and, therefore, minimize the losses to U. S. taxpayers. Instructions

Explain how reported accounting numbers might affect an individual's perceptions and actions. Cite two examples.

CA1-7 (Need for GAAP) Some argue that having various organizations establish accounting principles is wasteful and inefficient. Rather than mandating accounting rules, each company could voluntarily disclose the type of information it considered important. In addition, if an investor wants additional information, the investor could contact the company and pay to receive the additional information desired. Instructions

Comment on the appropriateness of this viewpoint.

CA1-8 (AICPA's Role in Rule-Making) One of the major groups involved in the standard-setting process is the American Institute of Certified Public Accountants. Initially, it was the primary organization that established accounting principles in the United States. Subsequently, it relinquished its power to the FASB. Instructions

(a) Identify the two committees of the AICPA that established accounting principles prior to the establishment of the FASB.



(b) Speculate as to why these two organizations failed. In your answer, identify steps the FASB has taken to avoid failure.

(c) What is the present role of the AICPA in the rule-making environment?

CA1-9 (FASB Role in Rule-Making) A press release announcing the appointment of the trustees of the new Financial Accounting Foundation stated that the Financial Accounting Standards Board (to be appointed by the trustees) “. . . will become the established authority for setting accounting principles under which corporations report to the shareholders and others” (AICPA news release July 20, 1972). Instructions

(a) Identify the sponsoring organization of the FASB and the process by which the FASB arrives at a decision and issues an accounting standard.

(b) Indicate the major types of pronouncements issued by the FASB and the purposes of each of these pronouncements.

CA1-10 (Politicization of GAAP) Some accountants have said that politicization in the development and acceptance of generally accepted accounting principles (i. e., rule-making) is taking place. Some use the term “politicization” in a narrow sense to mean the influence by governmental agencies, particularly the Securities and Exchange Commission, on the development of generally accepted accounting principles. Others use it more broadly to mean the compromise that results when the bodies responsible for developing generally accepted accounting principles are pressured by interest groups (SEC, American Accounting Association, businesses through their various organizations, Institute of Management Accountants, financial analysts, bankers, lawyers, and so on).

## Instructions

(a) The Committee on Accounting Procedure of the AICPA was established in the mid- to late 1930s and functioned until 1959, at which time the Accounting Principles Board came into existence. In 1973, the Financial Accounting Standards Board was formed and the APB went out of existence. Do the reasons these groups were formed, their methods of operation while in existence, and the reasons for the demise of the first two indicate an increasing politicization (as the term is used in the broad sense) of accounting standard-setting? Explain your answer by indicating how the CAP, the APB, and the FASB operated or operate. Cite specific developments that tend to support your answer. (b) What arguments can be raised to support the “ politicization” of accounting rule-making? (c) What arguments can be raised against the “ politicization” of accounting rule-making? (CMA adapted)

CA1-11 (Models for Setting GAAP) Presented below are three models for setting GAAP. 1. The purely political approach, where national legislative action decrees GAAP. 2. The private, professional approach, where GAAP is set and enforced by private professional actions only.

3. The public/private mixed approach, where GAAP is basically set by private-sector bodies that behave as though they were public agencies and whose standards to a great extent are enforced through governmental agencies.

## Instructions

(a) Which of these three models best describes standard-setting in the United States? Comment on your answer.

(b) Why do companies, financial analysts, labor unions, industry trade

associations, and others take such an active interest in standard-setting?

(c) Cite an example of a group other than the FASB that attempts to establish accounting standards. Speculate as to why another group might wish to set its own standards. CA1-12 (GAAP Terminology) Wayne Rogers, an administrator at a major university, recently said, " I've got some CDs in my IRA, which I set up to beat the IRS." As elsewhere, in the world of accounting and finance, it often helps to be fluent in abbreviations and acronyms.

### Instructions

Presented below is a list of common accounting acronyms. Identify the term for which each acronym stands, and provide a brief definition of each term.

- (a) AICPA (e) FAF (i) CPA
- (b) CAP (f) FASAC (j) FASB
- (c) ARB (g) SOP (k) SEC
- (d) APB (h) GAAP (l) IASB

CA1-13 (Accounting Organizations and Documents Issued) Presented below are a number of accounting organizations and types of documents they have issued.

### Instructions

Match the appropriate document to the organization involved. Note that more than one document may be issued by the same organization. If no document is provided for an organization, write in " 0." Organization

### Document

1. \_\_\_\_ Accounting Standards Executive Committee (a) Opinions 2. \_\_\_\_ Accounting Principles Board (b) Practice Bulletins
3. \_\_\_\_ Committee on Accounting Procedure (c) Accounting Research

Bulletins 4. \_\_\_\_\_ Financial Accounting Standards Board (d) Financial Accounting Standards (e) Statements of Position

CA1-14 (Accounting Pronouncements) Standard-setting bodies have issued a number of authoritative pronouncements. A list is provided on the left, below, with a description of these pronouncements on the right. Instructions

Match the description to the pronouncements.

1. \_\_\_\_\_ Staff Positions
2. \_\_\_\_\_ Interpretations (of the Financial Accounting Standards Board) 3. \_\_\_\_\_ Statement of Financial Accounting Standards
4. \_\_\_\_\_ EITF Statements
5. \_\_\_\_\_ Opinions
6. \_\_\_\_\_ Statement of Financial Accounting

Concepts

Concepts for Analysis 27

- (a) Official pronouncements of the APB.
- (b) Sets forth fundamental objectives and concepts that will be used in developing future standards.
- (c) Primary document of the FASB that establishes GAAP.
- (d) Provides additional guidance on implementing or applying FASB Standards or Interpretations.
- (e) Provides guidance on how to account for new and unusual financial transactions that have the potential for creating diversity in financial reporting practices.
- (f) Represent extensions or modifications of existing standards.

CA1-15 (Rule-Making Issues) When the FASB issues new pronouncements,

<https://assignbuster.com/fasb-codification-essay-sample/>

the implementation date is usually 12 months from date of issuance, with early implementation encouraged. Karen Weller, controller, discusses with her financial vice president the need for early implementation of a rule that would result in a fairer presentation of the company's financial condition and earnings. When the financial vice president 28 Chapter 1 Financial Accounting and Accounting Standards

determines that early implementation of the rule will adversely affect the reported net income for the year, he discourages Weller from implementing the rule until it is required. Instructions

Answer the following questions.

(a) What, if any, is the ethical issue involved in this case? (b) Is the financial vice president acting improperly or immorally? (c) What does Weller have to gain by advocacy of early implementation? (d) Which stakeholders might be affected by the decision against early implementation? (CMA adapted)

CA1-16 (Securities and Exchange Commission) The U. S. Securities and Exchange Commission (SEC) was created in 1934 and consists of five commissioners and a large professional staff. The SEC professional staff is organized into five divisions and several principal offices. The primary objective of the SEC is to support fair securities markets. The SEC also strives to foster enlightened stockholder participation in corporate decisions of publicly traded companies. The SEC has a significant presence in financial markets, the development of accounting practices, and corporation-shareholder relations, and has the power to exert influence on entities whose actions lie within the scope of its authority. Instructions

(a) Explain from where the Securities and Exchange Commission receives its authority. (b) Describe the official role of the Securities and Exchange Commission in the development of financial accounting theory and practices.

(c) Discuss the interrelationship between the Securities and Exchange Commission and the Financial Accounting Standards Board with respect to the development and establishment of financial accounting theory and practices.

(CMA adapted)

CA1-17 (Rule-Making Process) In 1973, the responsibility for developing and issuing rules on accounting practices was given to the Financial Accounting Foundation and, in particular, to an arm of the foundation called the Financial Accounting Standards Board (FASB). The generally accepted accounting principles established by the FASB are enunciated through a publication series entitled Statements of Financial Accounting Standards. These statements are issued periodically, and over 160 have been issued. The statements have a significant influence on the way in which financial statements are prepared by U. S. corporations. Instructions

(a) Describe the process by which a topic is selected or identified as appropriate for study by the Financial Accounting Standards Board (FASB). (b) Once a topic is considered appropriate for consideration by the FASB, a series of steps is followed before a Statement of Financial Accounting Standards is issued. Describe the major steps in the process leading to the issuance of a standard.

(c) Identify at least three other organizations that influence the setting of generally accepted accounting principles (GAAP).

(CMA adapted)

CA1-18 (Financial Reporting Pressures) Presented below is abbreviated testimony from Troy Normand in the WorldCom case. He was a manager in the corporate reporting department and is one of five individuals who pleaded guilty. He is testifying in hopes of receiving no prison time when he is ultimately sentenced.

Q. Mr. Normand, if you could just describe for the jury how the meeting started and what was said during the meeting?

A. I can't recall exactly who initiated the discussion, but right away Scott Sullivan acknowledged that he was aware we had problems with the entries, David Myers had informed him, and we were considering resigning. He said that he respected our concerns but that we weren't being asked to do anything that he believed was wrong. He mentioned that he acknowledged that the company had lost focus quite a bit due to the preparations for the Sprint merger, and that he was putting plans in place and projects in place to try to determine where the problems were, why the costs were so high. He did say he believed that the initial statements that we produced, that the line costs in those statements could not have been as high as they were, that he believed something was wrong and there was no way that the costs were that high.

I informed him that I didn't believe the entry we were being asked to do was right, that I was scared, and I didn't want to put myself in a position of going to jail for him or the company. He responded that he didn't believe anything

<https://assignbuster.com/fasb-codification-essay-sample/>

was wrong, nobody was going to be going to jail, but that if it later was found to be wrong, that he would be the person going to jail, not me.

He asked that I stay, don't jump off the plane, let him land it softly, that's basically how he put it. And he mentioned that he had a discussion with Bernie Ebbers, asking Bernie to reduce projections going forward and that Bernie had refused.

Q. Mr. Normand, you said that Mr. Sullivan said something about don't jump out of the plane. What did you understand him to mean when he said that?

A. Not to quit.

Q. During this meeting, did Mr. Sullivan say anything about whether you would be asked to make entries like this in the future?

A. Yes, he made a comment that from that point going forward we wouldn't be asked to record any entries, high-level late adjustments, that the numbers would be the numbers. Q. What did you understand that to be mean, the numbers would be the numbers? A. That after the preliminary statements were issued, with the exception of any normal transaction, valid transaction, we wouldn't be asked to be recording any more late entries. Q. I believe you testified that Mr. Sullivan said something about the line cost numbers not being accurate. Did he ask you to conduct any analysis to determine whether the line cost numbers were accurate? A. No, he did not.

Q. Did anyone ever ask you to do that?

A. No.

Q. Did you ever conduct any such analysis?



A. No, I didn't.

Q. During this meeting, did Mr. Sullivan ever provide any accounting justification for the entry you were asked to make?

A. No, he did not.

Q. Did anything else happen during the meeting?

A. I don't recall anything else.

Q. How did you feel after this meeting?

A. Not much better actually. I left his office not convinced in any way that what we were asked to do was right. However, I did question myself to some degree after talking with him wondering whether I was making something more out of what was really there.

#### Instructions

Answer the following questions.

- (a) What appears to be the ethical issue involved in this case?
- (b) Is Troy Normand acting improperly or immorally?
- (c) What would you do if you were Troy Normand?
- (d) Who are the major stakeholders in this case?

CA1-19 (Economic Consequences) Presented below are comments made in the financial press. Instructions

Prepare responses to the requirements in each item.

- (a) Rep. John Dingell, the ranking Democrat on the House Commerce Committee, threw his support behind the FASB's controversial derivatives accounting standard and encouraged the FASB to adopt the rule promptly.

Indicate why a member of Congress might feel obligated to comment on this proposed FASB standard.

(b) In a strongly worded letter to Senator Lauch Faircloth (R-NC) and House Banking Committee Chairman Jim Leach (R-IA), the American Institute of Certified Public Accountants (AICPA) cautioned against government intervention in the accounting standard-setting process, warning that it had the potential of jeopardizing U. S. capital markets. Explain how government intervention could possibly affect capital markets adversely.

CA1-20 (GAAP and Economic Consequences) The following letter was sent to the SEC and the FASB by leaders of the business community.

Dear Sirs:

The FASB has been struggling with accounting for derivatives and hedging for many years. The FASB has now developed, over the last few weeks, a new approach that it proposes to adopt as a final standard. We understand that the Board intends to adopt this new approach as a final standard without exposing it for public comment and debate, despite the evident complexity of the new approach, the speed with which it has been developed and the significant changes to the exposure draft since it was released more than one year ago. Instead, the Board plans to allow only a brief review by selected Concepts for Analysis 29

30 Chapter 1 Financial Accounting and Accounting Standards

parties, limited to issues of operationality and clarity, and would exclude questions as to the merits of the proposed approach.

As the FASB itself has said throughout this process, its mission does not

permit it to consider matters that go beyond accounting and reporting considerations. Accordingly, the FASB may not have adequately considered the wide range of concerns that have been expressed about the derivatives and hedging proposal, including concerns related to the potential impact on the capital markets, the weakening of companies' ability to manage risk, and the adverse control implications of implementing costly and complex new rules imposed at the same time as other major initiatives, including the Year 2000 issues and a single European currency. We believe that these crucial issues must be considered, if not by the FASB, then by the Securities and Exchange Commission, other regulatory agencies, or Congress.

We believe it is essential that the FASB solicit all comments in order to identify and address all material issues that may exist before issuing a final standard. We understand the desire to bring this process to a prompt conclusion, but the underlying issues are so important to this nation's businesses, the customers they serve and the economy as a whole that expediency cannot be the dominant consideration. As a result, we urge the FASB to expose its new proposal for public comment, following the established due process procedures that are essential to acceptance of its standards, and providing sufficient time to affected parties to understand and assess the new approach. We also urge the SEC to study the comments received in order to assess the impact that these proposed rules may have on the capital markets, on companies' risk management practices, and on management and financial controls. These vital public policy matters deserve consideration as part of the Commission's oversight responsibilities.

We believe that these steps are essential if the FASB is to produce the best possible accounting standard while minimizing adverse economic effects and maintaining the competitiveness of U. S. businesses in the international marketplace.

Very truly yours,

(This letter was signed by the chairs of 22 of the largest U. S. companies.)

Instructions

Answer the following questions.

- (a) Explain the “ due process” procedures followed by the FASB in developing a financial reporting standard.
- (b) What is meant by the term “ economic consequences” in accounting standard-setting? (c) What economic consequences arguments are used in this letter? (d) What do you believe is the main point of the letter?
- (e) Why do you believe a copy of this letter was sent by the business community to influential members of the U. S. Congress?

FINANCIAL REPORTING

Financial Reporting Problem

Beverly Crusher, a new staff accountant, is confused because of the complexities involving accounting standard-setting. Specifically, she is confused by the number of bodies issuing financial reporting standards of one kind or another and the level of authoritative support that can be attached to these reporting standards. Beverly decides that she must review the environment in which accounting standards are set, if she is to increase her understanding of the accounting profession.

Beverly recalls that during her accounting education there was a chapter or two regarding the environment of financial accounting and the development of GAAP. However, she remembers that her instructor placed little emphasis on these chapters. USING YOUR JUDGMENT

#### Instructions

(a) Help Beverly by identifying key organizations involved in accounting rule-making. (b) Beverly asks for guidance regarding authoritative support.

Please assist her by explaining what is meant by authoritative support.

(c) Give Beverly a historical overview of how rule-making has evolved so that she will not feel that she is the only one to be confused.

(d) What authority for compliance with GAAP has existed throughout the history of rulemaking? BRIDGE TO THE PROFESSION

#### Professional Research

As a newly enrolled accounting major, you are anxious to better understand accounting institutions and sources of accounting literature. As a first step, you decide to explore the FASB Conceptual Framework.

#### Instructions

If your school has a subscription to the FASB Codification, go to <http://aaahq.org/asclgin.cfm> to log in and access the FASB conceptual framework. When you have accessed the documents, you can use the search tool in your Internet browser to respond to the following items. (Provide paragraph citations.)

(a) What is the objective of financial reporting?

(b) What other means are there of communicating information, besides financial statements? (c) Indicate some of the users and the information they are most directly concerned with in economic decision-making.