

Development of accounting theory case flashcard



**ASSIGN
BUSTER**

THE DEVELOPMENT OF ACCOUNTING THEORY a. Explain the meaning of the term accounting principles as used in the audit report.

(Do not in this part discuss the significance of generally accepted. ") Answer:

Before I dissect the term " accounting principle," I first want to provide a brief definition of (1) accounting and (2) a principle. Accounting is the systematic recording, reporting, and analysis of financial transactions of a business and a principle is a rule or ethical standard. The definition of an accounting principle is a principle that governs current accounting practice and that is used as a reference to determine the appropriate treatment of complex transactions (InvestorWords. com).

In the audit report, the term accounting principle is referred to the rules and ethical standards that are used to provide reasonable and reliable assurance that the maintenance of records are accurately reflecting the transparency of any transactions and dispositions that occurred in the current year, that company operations were authorized and approved by management and directors of the respective company, and there is assurance that any unauthorized occurrences that may have a material effect on the financial statements have been prevented. . The president wants to know how you determine whether or not an accounting principle is generally accepted. Discuss the sources of evidence for determining whether an accounting principle has substantial authoritative support. Do not merely list the titles of publications.

Answer: In determining whether or not an accounting principle is generally accepted, there are four different sources of evidence for the determination

of substantial authoritative support: (1) AICPA Accounting Research Bulletins and Accounting Principles Board Opinions not superseded by action of the FASB, FASB Statements of Financial Accounting Standards and Interpretations, FASB Statement 133 Implementation Issues, and FASB Staff Positions, (2) FASB Technical Bulletins and, if cleared by the FASB, AICPA Industry Audit and Accounting Guides and Statements of Position, (3) AICPA Accounting Standards Executive Committee Practice Bulletins that have been cleared by the FASB and consensus positions of the FASB Emerging Issues Task Force (EITF), and (4) Implementation guides published by the FASB staff, AICPA accounting interpretations, and practices that are widely recognized and prevalent either generally or in the industry. The AICPA and FASB are These sources of evidence are reliable and respected among any prudent user of financial statements, but it is difficult to determine the “ general acceptance” of a particular accounting principle because there is no single reference source for all principles. c. The president believes that diversity in accounting practice will always exist among independent entities despite continual improvements in comparability. Discuss the arguments that support his belief.

Answer: Diversity in accounting practice will always exist among independent entities despite continual improvements in comparability because management is allowed too much leeway in the selection of the accounting procedures used in corporate financial reports. The two criticisms stated: (1) Executive compensation is frequently tied to reported earnings, so management is inclined to adopt accounting principles that increase current revenues and decrease current expenses. Thus, managers will

continuously seek different measurement and disclosure methods in order to increase current revenues and decrease current expenses. Our economy is based on a capitalistic society that will further increase due diligence in finding new methods for any improvement in their financial statements to alleviate the pressure placed on executives on revenue and earnings performance. (2) The value of a firm in the marketplace is determined by its stock price. This value of a firm in the marketplace is determined by its stock price where its value is highly influenced by financial analysts' quarterly earnings estimates.

Managers are fearful that failing to meet these earnings estimates will trigger a sell-off of the company's stock and resultant decline in the market value of the firm. Again, this second criticism is directly related to our capitalistic society. Managers are looking for alternative methods to better "manage" their earnings. Lastly, I believe that the volatility of the markets influences diversity in accounting practices as well.