

CHAPTER 1

FINANCIAL ACCOUNTING AND ACCOUNTING STANDARDS

IFRS questions are available at the end of this chapter.

TRUE-FALSE—Conceptual

Answer	No.	Description
F	1.	Definition of financial accounting.
T	2.	Purpose of financial statements.
T	3.	Definition of financial accounting.
T	4.	Capital allocation process.
F	5.	Objective of financial reporting.
T	6.	Decision-Usefulness approach.
T	7.	Users of financial statements.
F	8.	Committee on Accounting Procedure.
F	9.	Passage of new FASB statement.
T	10.	Statements of Financial Accounting Concepts.
T	11.	Creation of Accounting Principles Board.
F	12.	FASB Codification.
T	13.	Code of Professional Conduct.
F	14.	GAAP and political action.
T	15.	Public Company Accounting Oversight Board.
T	16.	Expectations gap.
F	17.	Financial reports.
F	18.	Fair value information.
F	19.	International Financial Reporting Standards.
F	20.	Ethical issues.

MULTIPLE CHOICE—Conceptual

Answer	No.	Description
a	21.	Financial accounting.
d	22.	Users of financial reports.
d	23.	Identify the major financial statements.
a	24.	Financial reporting entity.
d	25.	Differences between financial and managerial accounting.
b	26.	Financial reporting communication.
b	27.	Managerial accounting.
a	28.	Capital allocation process.
d	29.	Efficient use of resources.
d	30.	Capital allocation process.
c	31.	Financial statement information.
c	32.	Accounting profession challenge.
c	33.	Financial reporting objective.
d	34.	Financial statements primary users.
c	35.	Investor's decision making.

MULTIPLE CHOICE—Conceptual (cont.)

Answer	No.	Description
b	36.	Accrual accounting.
c	37.	Entity perspective.
c	38.	Meaning of "generally accepted."
b	39.	Common set of standards and procedures.
a	40.	Limitation of general purpose financial statements.
c	41.	Securities and Exchange Commission and accounting standard setting.
d	42.	Due process in FASB standard setting.
d	43.	Organizations responsible for setting accounting standards.
b	44.	Reason for Accounting Principles Board creation
b	45.	Organization issuing Accounting Research Bulletins.
a	46.	Characteristic of GAAP.
c	47.	Characteristics of GAAP.
d	48.	FASB accounting standards.
c	49.	FASB standard passage.
b	50.	Purpose of Emerging Issues Task Force.
a	51.	AICPA role in standard setting.
c	52.	Role of SEC.
c	53.	Powers of the SEC.
d	54.	SEC enforcement.
d	55.	Creation of FASB.
d	56.	Appointment of FASB members.
a	57.	Purpose of the Financial Accounting Foundation.
b	58.	Characteristics of FASB.
b	59.	FASB and "due process" system.
b	60.	Publications of FASB.
c	61.	Purpose of FASB Technical Bulletins.
d	62.	Purpose of Emerging Issues Task Force.
b	63.	Role of the AICPA.
b	64.	Pronouncement issued by the APB.
c	65.	Standard setting organizations.
d	66.	Identification of standard setting organizations.
c	67.	Statements of financial accounting concepts.
d	^P 68.	FASB members.
d	^P 69.	FASB statement process.
d	70.	Nature of GAAP.
d	71.	Body which promulgates GAAP.
d	72.	Publications which are not GAAP.
d	73.	Publications which are not GAAP.
b	74.	Code for Professional Conduct Rule 203.
c	75.	Purpose of FASB staff position.
c	76.	Components of GAAP.
a	77.	Political environment of standard setting.
c	78.	International Accounting Standards Board.

MULTIPLE CHOICE—Conceptual (cont.)

Answer	No.	Description
d	79.	Standard setting process pressure.
a	80.	Danger of politics in standard setting
c	81.	Definition of "expectation gap".
b	82.	Reason accounting standards differ across countries.
d	83.	Advantage of countries adopting same accounting standards.
a	84.	Ethical concern of accountants.

^P Note: these questions also appear in the Problem-Solving Survival Guide.

EXERCISES

Item	Description
E1-85	Objectives of financial reporting.
E1-86	Development of accounting principles.
E1-87	Publications and organizations.
E1-88	FASB.
E1-89	Evolution of a statement of financial accounting standards.

CHAPTER LEARNING OBJECTIVES

1. Identify the major financial statements and other means of financial reporting.
2. Explain how accounting assists in the efficient use of scarce resources.
3. Identify the objective of financial reporting.
4. Explain the need for accounting standards.
5. Identify the major policy-setting bodies and their role in the standard-setting process.
6. Explain the meaning of generally accepted accounting principles (GAAP) and the role of the Codification for GAAP.
7. Describe the impact of user groups on the rule-making process.
8. Describe some of the challenges facing financial reporting.
9. Understand issues related to ethics and financial accounting.

SUMMARY OF LEARNING OBJECTIVES BY QUESTIONS

Item	Type	Item	Type	Item	Type	Item	Type	Item	Type	Item	Type	Item	Type
Learning Objective 1													
1.	TF	21.	MC	23.	MC	25.	MC	^P 27.	MC				
2.	TF	22.	MC	24.	MC	26.	MC						
Learning Objective 2													
3.	TF	4.	TF	28.	MC	29.	MC	30.	MC				
Learning Objective 3													
5.	TF	33.	MC	35.	MC	37.	MC						
6.	TF	34.	MC	36.	MC	85.	E						
Learning Objective 4													
7.	TF	38.	MC	39.	MC	40.	MC	86.	E				
Learning Objective 5													
8.	TF	43.	MC	49.	MC	55.	MC	61.	MC	67.	MC	89.	E
9.	TF	44.	MC	50.	MC	56.	MC	62.	MC	^P 68.	MC		
10.	TF	45.	MC	51.	MC	57.	MC	63.	MC	^P 69.	MC		
11.	TF	46.	MC	52.	MC	58.	MC	64.	MC	^P 86.	E		
41.	MC	47.	MC	53.	MC	59.	MC	65.	MC	87.	E		
42.	MC	48.	MC	54.	MC	60.	MC	66.	MC	88.	E		
Learning Objective 6													
12.	TF	70.	MC	72.	MC	74.	MC	76.	MC				
13.	TF	71.	MC	73.	MC	75.	MC						
Learning Objective 7													
14.	TF	16.	TF	77.	MC	79.	MC	81.	MC	83.	E		
15.	TF	62.	MC	78.	MC	80.	MC	82.	MC				
Learning Objective 8													
17.	TF	18.	TF	19.	TF	31.	MC	32.	MC				
Learning Objective 9													
20.	TF	84.	MC										

Note: TF = True-False
 MC = Multiple Choice
 E = Exercise

TRUE-FALSE—Conceptual

1. Financial accounting is the process of identifying, measuring, analyzing, and communicating financial information needed by management to plan, evaluate, and control a company's operations.
2. Financial statements are the principal means through which a company communicates its financial information to those outside it.
3. Users of financial reports of a company use the information provided by these reports to make their capital allocation decisions.
4. An effective process of capital allocation promotes productivity and provides an efficient market for buying and selling securities and obtaining and granting credit.
5. The objective of financial reporting is to report the plans made by a company to improve the productivity of its employees.
6. Investors are interested in financial reporting because it provides information that is useful for making decisions.
7. Users of financial accounting statements have both coinciding and conflicting needs for information of various types.
8. The Securities and Exchange Commission appointed the Committee on Accounting Procedure.
9. The passage of a new FASB Accounting Standards Update requires the support of five of the seven board members.
10. Statements of Financial Accounting Concepts set forth fundamental objectives and concepts that are used by the FASB in developing future standards of financial accounting and reporting.
11. The AICPA created the Accounting Principles Board in 1959.
12. The FASB's Codification creates a new set of GAAP.
13. The AICPA's Code of Professional Conduct requires that members prepare financial statements in accordance with generally accepted accounting principles.
14. GAAP is a product of careful logic or empirical findings and is not influenced by political action.
15. The Public Company Accounting Oversight Board has oversight and enforcement authority and establishes auditing and independence standards and rules.
16. The expectations gap is due to the difference between what the public thinks accountants should do and what accountants think they can do.

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17. Financial reports in the early 21st century did not provide any information about a company's soft assets (intangibles).
18. Accounting standards are now less likely to require the recording or disclosure of fair value information.
19. U.S. companies that list overseas are required to use International Financial Reporting Standards, issued by the International Accounting Standards Board.
20. Ethical issues in financial accounting are governed by the AICPA.

True-False Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
1.	F	6.	T	11.	T	16.	T
2.	T	7.	T	12.	F	17.	F
3.	T	8.	F	13.	T	18.	F
4.	T	9.	F	14.	F	19.	F
5.	F	10.	T	15.	T	20.	F

MULTIPLE CHOICE—Conceptual

21. General-purpose financial statements are the product of
 - a. financial accounting.
 - b. managerial accounting.
 - c. both financial and managerial accounting.
 - d. neither financial nor managerial accounting.
22. Which of the following is **not** a user of financial reports?
 - a. Creditors.
 - b. Government agencies.
 - c. Unions.
 - d. All of these are users.
23. The financial statements most frequently provided include all of the following **except** the
 - a. balance sheet.
 - b. income statement.
 - c. statement of cash flows.
 - d. statement of retained earnings.
24. The information provided by financial reporting pertains to
 - a. individual business enterprises, rather than to industries or an economy as a whole or to members of society as consumers.
 - b. business industries, rather than to individual enterprises or an economy as a whole or to members of society as consumers.
 - c. individual business enterprises, industries, and an economy as a whole, rather than to members of society as consumers.
 - d. an economy as a whole and to members of society as consumers, rather than to individual enterprises or industries.

25. All the following are differences between financial and managerial accounting in how accounting information is used **except** to
- plan and control company's operations.
 - decide whether to invest in the company.
 - evaluate borrowing capacity to determine the extent of a loan to grant.
 - All the answer choices are correct.
26. Which of the following represents a form of communication through financial reporting but not through financial statements?
- Balance sheet.
 - President's letter.
 - Income statement.
 - Notes to financial statements.
- P27. The process of identifying, measuring, analyzing, and communicating financial information needed by management to plan, evaluate, and control an organization's operations is called
- financial accounting.
 - managerial accounting.
 - tax accounting.
 - auditing.
28. How does accounting help the capital allocation process attract investment capital?
- By providing timely, relevant information.
 - By encouraging innovation.
 - By promoting productivity.
 - By providing timely, relevant information and by encouraging innovation.
29. Which of the following helps in determining whether a business thrives?
- Markets.
 - Free enterprise.
 - Competition.
 - All of these answer choices are correct.
30. Which of the following is related to an effective capital allocation?
- Promoting productivity.
 - Encouraging innovation.
 - Providing an efficient market for buying and selling securities.
 - All of these answer choices are correct.
31. Financial statements in the early 2000s provide information related to
- nonfinancial measurements.
 - forward-looking data.
 - hard assets (inventory and plant assets).
 - None of these answer choices are correct.
32. Which of the following is **not** a major challenge facing the accounting profession?
- Nonfinancial measurements.
 - Timeliness.
 - Accounting for hard assets.
 - Forward-looking information.

33. What is the objective of financial reporting?
- Provide information that is useful to management in making decisions.
 - Provide information that clearly portrays nonfinancial transactions.
 - Provide information about the reporting entity that is useful to present and potential equity investors, lenders, and other creditors.
 - Provide information that excludes claims to the resources.
34. Primary users for general-purpose financial statements include
- creditors.
 - employees.
 - investors.
 - both creditors and investors.
35. Which of the following will be of interest to investors in decision-making?
- Assessing the company's ability to generate net cash inflows.
 - Assessing management's ability to protect and enhance the capital providers' investments.
 - Both assessing the company's ability to generate net cash inflows and assessing management's ability to protect and enhance the capital provider's investments.
 - Assessing the company's ability to collect debts.
36. Accrual accounting is used because
- cash flows are considered less important.
 - it provides a better indication of a company's ability to generate cash flows than the cash basis.
 - it recognizes revenues when cash is received and expenses when cash is paid.
 - None of the answer choices are correct.
37. Which perspective is adopted as a part of the objective of general-purpose financial reporting?
- A decision-usefulness perspective.
 - A proprietary perspective.
 - An entity perspective.
 - A financial reporting perspective.
38. Which of the following is a requirement for an accounting principle to be called "generally accepted"?
- An authoritative accounting rule-making body has established it in an official pronouncement.
 - The principle has been accepted as appropriate because of its universal application.
 - An authoritative accounting rule-making body has established it and it has been accepted because of its universal application.
 - None of the answer choices are correct.
39. A common set of accounting standards and procedures are called
- financial accounting standards.
 - generally accepted accounting principles.
 - objectives of financial reporting.
 - statements of financial accounting concepts.

40. Which of the following is a general limitation of "general purpose financial statements"?
- General purpose financial statements may not be the most informative for a specific enterprise.
 - General purpose financial statements are not comparable.
 - General purpose financial statements do not fairly present a company's financial operations.
 - None of the answer choices are correct.
41. What is the relationship between the Securities and Exchange Commission and accounting standard setting in the United States?
- The SEC requires all companies listed on an exchange to submit their financial statements to the SEC.
 - The SEC coordinates with the AICPA in establishing accounting standards.
 - The SEC has a mandate to establish accounting standards for enterprises under its jurisdiction.
 - The SEC reviews financial statements for compliance.
42. What is due process in the context of standard setting at the FASB?
- The FASB operates in full view of the public.
 - Public hearings are held on proposed accounting standards.
 - Interested parties can make their views known.
 - All of the answer choices are correct.
43. Which of the following organizations has been responsible for setting U.S. accounting standards?
- The Accounting Principles Board.
 - The Committee on Accounting Procedure.
 - The Financial Accounting Standards Board.
 - All of the answer choices are correct.
44. Why did the AICPA create the Accounting Principles Board?
- The SEC disbanded the previous standard setting organization.
 - The previous standard setting organization did not provide a structured set of accounting principles.
 - No such organization existed in the past.
 - None of the answer choices are correct.
45. Which organization was responsible for issuing Accounting Research Bulletins?
- The Accounting Principles Board.
 - The Committee on Accounting Procedure.
 - The SEC.
 - The FASB.
46. A characteristic of generally accepted accounting principles include:
- a common set of standards and principles.
 - standards and principles are based a federal statutes.
 - acceptance requires an affirmative vote of Certified Public Accountants.
 - practices that become accepted for at least a year by all industry members.

47. Characteristics of generally accepted accounting principles include all of the following **except**
- authoritative accounting that the rule-making body has established as a principle of reporting.
 - standards are considered useful by the profession.
 - each principle is approved by the SEC.
 - practice has become universally accepted over time.
48. Why was it believed that accounting standards that were issued by the Financial Accounting Standards Board would carry more weight?
- Smaller membership.
 - The FASB board members were well-paid.
 - The FASB board members were CPAs.
 - Due process.
49. The passage of a new FASB Accounting Standards Update requires the support of
- seven Board members.
 - three Board members.
 - four Board members.
 - five Board members.
50. What is the purpose of Emerging Issues Task Force?
- Provide interpretation of existing standards.
 - Provide a consensus on how to account for new and unusual financial transactions.
 - Provide interpretive guidance.
 - Provide timely guidance on select issues.
51. Which organization is responsible for issuing Emerging Issues Task Force Statements?
- The FASB
 - The CAP
 - The APB
 - The SEC
52. The role of the Securities and Exchange Commission in the formulation of accounting principles can be best described as
- consistently primary.
 - consistently secondary.
 - sometimes primary and sometimes secondary.
 - non-existent.
53. The body that has the power to prescribe the accounting practices and standards to be employed by companies that fall under its jurisdiction is the
- FASB.
 - AICPA.
 - SEC.
 - APB.

54. Companies that are listed on a stock exchange are required to submit their financial statements to the
- AICPA.
 - APB
 - FASB.
 - SEC.
55. The Financial Accounting Standards Board (FASB) was proposed by the
- American Institute of Certified Public Accountants.
 - Accounting Principles Board.
 - Study Group on the Objectives of Financial Statements.
 - Study Group on establishment of Accounting Principles (Wheat Committee).
56. Which of the following is true of the Financial Accounting Standards Board
- It has issued a series of pronouncements entitled Auditing Standards Updates.
 - It was the forerunner of the current Accounting Principles Board.
 - It is the arm of the Securities and Exchange Commission responsible for setting financial accounting standards.
 - The members of the FASB are appointed by the Financial Accounting Foundation.
57. The Financial Accounting Foundation
- oversees the operations of the FASB.
 - oversees the operations of the AICPA.
 - provides information to interested parties on financial reporting issues.
 - works with the Financial Accounting Standards Advisory Council to provide information to interested parties on financial reporting issues.
58. The major distinction between the Financial Accounting Standards Board (FASB) and its predecessor, the Accounting Principles Board (APB), is
- the FASB issues exposure drafts of proposed standards.
 - all members of the FASB are fully remunerated, serve full time, and are independent of any companies or institutions.
 - all members of the FASB possess extensive experience in financial reporting.
 - a majority of the members of the FASB are CPAs drawn from public practice.
59. The Financial Accounting Standards Board employs a "due process" system which
- is an efficient system for collecting dues from members.
 - enables interested parties to express their views on issues under consideration.
 - identifies the accounting issues that are the most important.
 - requires that all accountants must receive a copy of financial standards.
60. Which of the following is **not** a publication of the FASB?
- Statements of Financial Accounting Concepts
 - Accounting Research Bulletins
 - Interpretations
 - Technical Bulletins

61. FASB Technical Bulletins
- are similar to FASB Interpretations in that they establish enforceable standards under the AICPA's Code of Professional Ethics.
 - are issued monthly by the FASB to deal with current topics.
 - are not expected to have a significant impact on financial reporting in general and provide guidance when it does not conflict with any broad fundamental accounting principle.
 - were recently discontinued by the FASB because they dealt with specialized topics having little impact on financial reporting in general.
62. The purpose of the Emerging Issues Task Force is to
- develop a conceptual framework as a frame of reference for the solution of future problems.
 - lobby the FASB on issues that affect a particular industry.
 - do research on issues that relate to long-term accounting problems.
 - issue statements which reflect a consensus on how to account for new and unusual financial transactions that need to be resolved quickly.
63. The American Institute of Certified Public Accountants (AICPA) continues to be involved in all of the following **except**
- developing and enforcing professional ethics.
 - developing auditing standards for public companies.
 - providing professional education programs.
 - All of the answer choices are correct.
- P64. Which of the following pronouncements were issued by the Accounting Principles Board?
- Accounting Research Bulletins
 - APB Opinions
 - APB Statements of Position
 - Statements of Financial Accounting Concepts
65. Which of the following organizations has **not** been instrumental in the development of financial accounting standards in the United States?
- AICPA
 - FASB
 - IASB
 - SEC
66. Which of the following organizations has **not** published accounting standards?
- American Institute of Certified Public Accountants.
 - Securities and Exchange Commission.
 - Financial Accounting Standards Board.
 - All of these have published accounting standards.
67. The purpose of Statements of Financial Accounting Concepts is to
- establish GAAP.
 - modify or extend an existing FASB Accounting Standards Update.
 - form a conceptual framework for solving existing and emerging problems.
 - determine the need for FASB involvement in an emerging issue.

- P68. Members of the Financial Accounting Standards Board are
- employed by the American Institute of Certified Public Accountants (AICPA).
 - part-time employees.
 - required to hold a CPA certificate.
 - independent of any other organization.
- P69. The following are part of the "due process" system used by the FASB in the evolution of a typical FASB Accounting Standards Update:
- Exposure Draft
 - FASB Accounting Standards Update
 - Preliminary Views
- The chronological order in which these items are released is as follows:
- 1, 2, 3.
 - 1, 3, 2.
 - 2, 3, 1.
 - 3, 1, 2.
70. Which of the following is true of generally accepted accounting principles?
- GAAP includes detailed practices and procedures as well as broad guidelines of general application.
 - GAAP is influenced by pronouncements of the SEC and IRS.
 - GAAP changes over time as the nature of the business environment changes.
 - All of these answer choices are correct.
71. The most significant current source of generally accepted accounting principles is the
- AICPA.
 - SEC.
 - APB.
 - FASB.
72. Which of the following is **not** a part of generally accepted accounting principles?
- The FASB Interpretations
 - The CAP Accounting Research Bulletins
 - The APB Opinions
 - All of these are part of generally accepted accounting principles.
73. Which of the following publications does **not** qualify as a statement of generally accepted accounting principles?
- Statements of financial standards issued by the FASB
 - Accounting interpretations issued by the FASB
 - APB Opinions
 - Accounting research studies issued by the AICPA
74. Rule 203 of the Code of Professional Conduct addresses:
- ethical requirements.
 - financial statements being based on generally accepted accounting principles.
 - advertising to obtain clients.
 - auditing financial statements.

75. What is the purpose of a FASB Staff Position?
- Provide interpretation of existing standards.
 - Provide a consensus on how to account for new and unusual financial transactions.
 - Provide interpretive guidance.
 - Provide timely guidance on select issues.
76. Which of the following is **not** considered a component of generally accepted accounting principles?
- FASB Implementation Guides.
 - Widely recognized industry practices.
 - Articles published in CPA journals.
 - AICPA Accounting Interpretations.
77. Financial accounting standard-setting in the United States
- can be described as a social process which reflects political actions of various interested user groups as well as a product of research and logic.
 - is based solely on research and empirical findings.
 - is a legalistic process based on rules promulgated by governmental agencies.
 - is democratic in the sense that a majority of accountants must agree with a standard before it becomes enforceable.
78. The purpose of the International Accounting Standards Board is to
- issue enforceable standards which regulate the financial accounting and reporting of multinational corporations.
 - develop a uniform currency in which the financial transactions of companies throughout the world would be measured.
 - promote uniform accounting standards among countries of the world.
 - arbitrate accounting disputes between auditors and international companies.
79. Which of the following is a source of pressure that may influence the accounting standard setting process?
- Congress.
 - Lobbyist.
 - CPA firms.
 - All of these answers are correct.
80. What is a possible danger if politics plays too big a role in accounting standard setting?
- Accounting standards that are not truly generally accepted.
 - Individuals may influence the standards.
 - User groups become active.
 - The FASB delegates its authority to elected officials.

81. What is the "expectations gap"?
- The difference between what the public thinks the accountant should not do and what the accountant knows they should do.
 - The difference between what the public thinks the accountant is doing and what Congress says the accountant is doing.
 - The difference between what the public thinks the accountant should do and what the accountant thinks they can do.
 - The difference between what the accountant is doing and what the Courts say the accountant should be doing.
82. What is **not** a reason that accounting standards may differ across countries?
- Governments.
 - Language.
 - Culture.
 - Past practice.
83. What would be an advantage of having all countries adopt and follow the same accounting standards?
- Agreement.
 - Comparability.
 - Lower preparation costs.
 - Comparability and lower preparation costs.
84. Which of the following is an ethical concern of accountants?
- Earnings manipulation.
 - Conservative accounting.
 - Industry practices.
 - None of these answers are correct.

Multiple Choice Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
21.	a	31.	c	41.	c	51.	a	61.	c	71.	d	81.	c
22.	d	32.	c	42.	d	52.	c	62.	d	72.	d	82.	b
23.	d	33.	c	43.	d	53.	c	63.	b	73.	d	83.	d
24.	a	34.	d	44.	b	54.	d	64.	b	74.	b	84.	a
25.	d	35.	c	45.	b	55.	d	65.	c	75.	c		
26.	b	36.	b	46.	a	56.	d	66.	d	76.	c		
27.	b	37.	c	47.	c	57.	a	67.	c	77.	a		
28.	a	38.	c	48.	d	58.	b	68.	d	78.	c		
29.	d	39.	b	49.	c	59.	b	69.	d	79.	d		
30.	d	40.	a	50.	b	60.	b	70.	d	80.	a		

EXERCISES

Ex. 1-85—Objective of financial reporting.

What is the objective of financial reporting? How do general-purpose financial statements help meet this objective.

Solution 1-85

The objective of 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. They help shareholders, creditors, employees, and regulators to better understand a company's financial position and related performance.

Ex. 1-86—Development of accounting principles.

Presented below are three independent, unrelated statements regarding the formulation of generally accepted accounting principles. Each statement contains some incorrect or debatable statement(s).

Statement I

The users of financial accounting statements have coinciding and conflicting needs for statements of various types. To meet these needs, and to satisfy the financial reporting responsibility of management, accountants prepare different sets of financial statements for different users.

Statement II

The FASB should be responsive to the needs and viewpoints of the entire economic community, not just the public accounting profession. The FASB therefore will succeed because it will deal effectively with all interested groups.

Statement III

The Securities and Exchange Commission is very concerned about financial reporting and has formulated a committee called the Accounting Standards Executive Committee (AcSEC). This will provide input to the FASB. In addition, after each FASB Statement is issued, the AcSEC issues Statements of Position stating its position on the FASB statement.

Instructions

Evaluate each of the independent statements and identify the areas of fallacious reasoning in each. Explain why the reasoning is incorrect. Complete your discussion of each statement before proceeding to the next statement.

Solution 1-86Statement I

It is true that users of financial accounting statements have coinciding and conflicting needs for statements of various types. However, to meet these needs, accountants generally prepare a single set of general-purpose financial statements, rather than a number of different types of financial statements. It may be argued that accountants often do prepare special statements for particular purposes, but in general the accounting profession has relied on general purpose financial statements prepared in conformance with generally accepted accounting principles.

Statement II

It is true that the FASB should be responsive to the needs of the entire economic community, not just the public accounting profession. However, it is not clear whether the FASB will succeed. The FASB will have the best chance of survival if it deals with problems promptly, sets proper priorities, takes whatever action it thinks is right and in the public interest, and handles pressures responsibly without overreacting to them.

Statement III

The Accounting Standards Executive Committee (AcSEC) was established within the American Institute of Certified Public Accountants, not the Securities and Exchange Commission, to respond to pronouncements of the FASB. The AcSEC does issue Statements of Position, but issues them before the FASB sets standards on the issue.

Ex. 1-87—Publications and organizations.

Significant accounting publications are listed below (1-8). Sources or sponsors of accounting publications are identified next by alphabetical character (a-e). Match the publications with their sources.

Publications

- ___ 1. Accounting Research Bulletins (1953-1959)
- ___ 2. Accounting Standards Updates
- ___ 3. Statements of Position (SOPs)
- ___ 4. Statements of Financial Accounting Concepts
- ___ 5. Opinions (1962-1973)

Sources/Sponsors

- a. Financial Accounting Standards Board
- b. Accounting Standards Executive Committee
- c. The AICPA
- d. Committee on Accounting Procedure
- e. Accounting Principles Board

Solution 1-87

- | | |
|------|------|
| 1. d | 4. a |
| 2. a | 5. e |
| 3. b | |

Ex. 1-88—FASB.

The Financial Accounting Standards Board was established because many groups interested in financial reporting believed that the Accounting Principles Board was not effective. Discuss the apparent advantages that the FASB should have over its earlier counterpart, the APB.

Solution 1-88

1. Smaller membership. The FASB is composed of seven members, replacing the relatively large 18-member APB.
2. Full-time, remunerated membership. FASB members are well-paid, full-time members, appointed for renewable five-year terms. The APB members were unpaid and part-time.
3. Greater autonomy. The APB was a senior committee of the AICPA, whereas the FASB is not part of any single professional organization. It is appointed by and answerable only to the Financial Accounting Foundation.
4. Increased independence. The APB members retained their private positions with firms, companies, or institutions. The FASB members must sever all such ties.
5. Broader representation. All APB members were required to be CPAs and members of the AICPA. Currently, it is not necessary to be a CPA to be a member of the FASB.

Ex. 1-89—Evolution of a statement of financial accounting standards.

In establishing financial accounting standards, two basic premises of the FASB are (1) The FASB should be responsive to the needs and viewpoints of the entire economic community, not just the 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. To ensure achievement of these goals, what are the steps taken in the evolution of an FASB Statement of Financial Accounting Standards?

Solution 1-89

The steps in the evolution of an FASB Accounting Standards Updates are:

- a. Topics are identified and placed on the Board's agenda.
- b. Research and analysis are conducted and preliminary views of pros and cons are issued.
- c. A public hearing on the proposed standard is held.
- d. The Board evaluates the research and public response and issues an exposure draft.
- e. The Board evaluates the responses and changes the exposure draft, if necessary. The final standard is then issued.

IFRS QUESTIONS

True/False:

1. IFRS includes both International Financial Reporting Standards and International Accounting Standards.
2. International Financial Reporting Standards preceded International Accounting Standards
3. The standard-setting structure used by the International Accounting Standards Board is very similar to that used by the Financial Accounting Standards Board.
4. The rules-based standards of IFRS are more detailed than the simpler, principles-based standards of U.S. GAAP.
5. The International Accounting Standards Board has seven members.
6. The internal control standards applicable to Sarbanes–Oxley (SOX) apply only to large public companies listed on U.S. exchanges.

Answers to True/False questions:

1. True
2. False
3. True
4. False
5. False
6. True

Multiple Choice:

7. Authoritative standards for IFRS include:
 - a. International Financial Reporting Standards only.
 - b. International Financial Reporting Standards and International Accounting Standards only.
 - c. International Financial Reporting Standards, International Accounting Standards and U.S. GAAP only.
 - d. International Financial Reporting Standards, International Accounting Standards and any GAAP standard recognized by an organized stock exchange.
8. Which of these statements regarding the IFRS and U.S. GAAP is correct?
 - a. U.S. GAAP is considered to be "principles-based".
 - b. U.S. GAAP is considered to be less detailed than IFRS.
 - c. IFRS is considered to be "principles-based" and less detailed than U.S. GAAP
 - d. Both U.S. GAAP and IFRS are considered to be "rules-based", but U.S. GAAP tends to be more complex.
9. The IASB's standard-setting structure includes all of the following **except**
 - a. the Standing Interpretations Committee
 - b. the Standards Advisory Council
 - c. the Standards Comparison Committee
 - d. the Trustees

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10. Which of the following organizations have committed to develop high-quality, compatible accounting standards that could be used for domestic and cross-border financial reporting
- The Financial Accounting Standards Board (FASB) and the International Organization of Securities Commission (IOSCO)
 - The Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB)
 - The International Accounting Standards Board (IASB) and International Organization of Securities Commission (IOSCO)
 - The International Accounting Standards Board (IASB) and the Standards Advisory Council (SAC)
11. Which of the following organizations is **not** among the four international standard-setting organizations?
- The International Accounting Standards Committee Foundation (IASCF)
 - The Standards Advisory Council (SAC)
 - The International Financial Reporting Interpretations Committee (IFRIC)
 - The Financial Executives Institute (FEI)
12. Which of the following organizations selects members for the IASB?
- The Accounting Standards Committee Foundation
 - The Standards Advisory Council
 - The International Financial Reporting Interpretations Committee
 - The International Accounting Standards Committee Foundation
13. The IASB consists of _____ part-time members.
- seven
 - two
 - three
 - five
14. The purpose of the International Accounting Standards Board is to:
- regulate stock prices at the international level.
 - develop a uniform currency in which the financial transactions occur.
 - develop a single set of high-quality financial reporting standards.
 - arbitrate accounting disputes between auditors and international companies.

Answers to Multiple Choice:

7. b 11. d
8. c 12. d
9. c 13. b
10. b 14. c

Short Answer:

15. Why would it be advantageous for U.S. GAAP and International GAAP to be the same?

Relevant and reliable financial information is a necessity for viable capital markets. Unfortunately, financial statements from companies outside the United States are often prepared using different principles than U.S. GAAP. As a result, international companies have to develop financial information in different ways. Beyond the additional costs these companies incur, users of financial statements are often forced to understand at least two sets of GAAP. It is not surprising that there is a growing demand for one set of high quality international standards.

16. What is the difference between principles-based and rules-based accounting rules? Is IFRS more principles-based than U.S. GAAP? Explain.

Principles-based rules are considered to be based on accounting principles to result in financial statements that are presented. Rules-based standards are generally quite detailed, and in many instances follow a “check-box” mentality that some contend may shield auditors and companies from legal liability. Because IFRS tends to be simpler and less stringent in its accounting and disclosure requirements, it is generally considered more principles-based than U.S. GAAP.