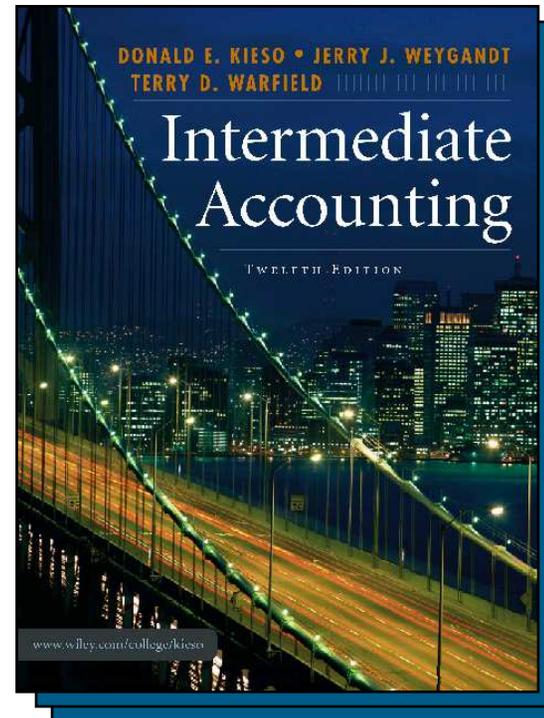


Full Disclosure: Concepts and Practices

Chapter 24

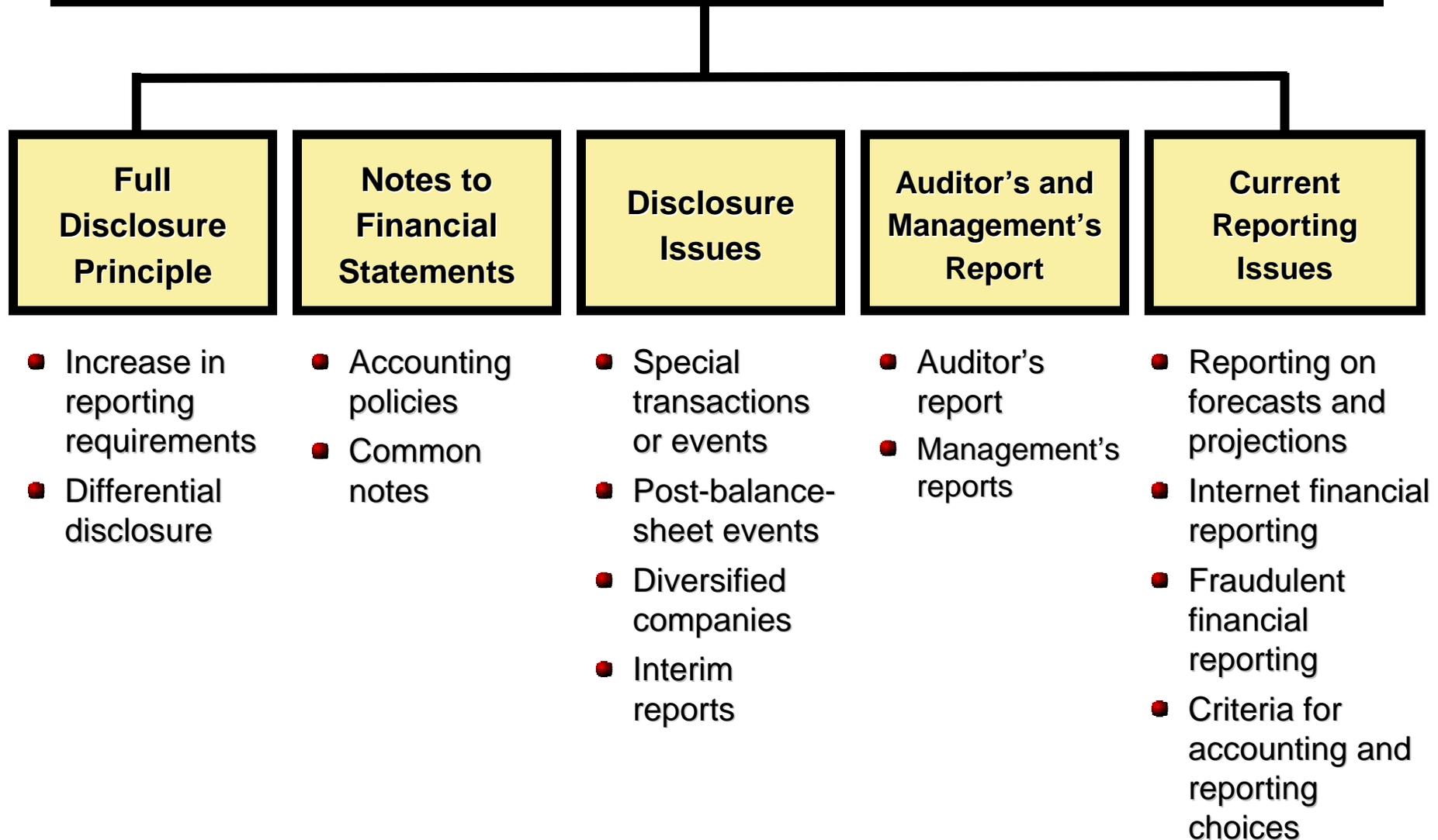
Intermediate Accounting
12th Edition
Kieso, Weygandt, and Warfield



Learning Objectives

1. Review the full disclosure principle and describe implementation problems.
2. Explain the use of notes in financial statement preparation.
3. Discuss the disclosure requirements for major business segments.
4. Describe the accounting problems associated with interim reporting.
5. Identify the major disclosures in the auditor's report.
6. Understand management's responsibilities for financials.
7. Identify issues related to financial forecasts and projections.
8. Describe the profession's response to fraudulent financial reporting.

Full Disclosure in Financial Reporting



Full Disclosure Principle

Full disclosure principle calls for financial reporting of any financial facts significant enough to influence the judgment of an informed reader.

Financial disasters at **Microstrategy**, **PharMor**, **WorldCom**, and **Global Crossing** highlight the difficulty of implementing the full disclosure principle.

Full Disclosure Principle

All Information Useful for Investment, Credit, and Similar Decisions

Financial Reporting

Affected by Existing FASB Standards

Basic Financial Statements

Illustration 24-1

Financial Statements

- Balance sheet
- Statement of Income
- Statement of Cash Flows
- Statement of Changes in Stockholders' Equity

Notes to Financial Statements

- Examples
- Accounting Policies
 - Contingencies
 - Inventory Methods
 - Shares Outstanding
 - Alternative Measures

Supplementary Information

- Examples:
- Changing Prices Disclosures
 - Oil and Gas Reserves Information

Other Means of Financial Reporting

- Examples:
- Management Discussion and Analysis
 - Letters to Stockholders

Other Information

- Examples:
- Competition and Order Backlog in SEC Forms
 - Analysts' reports
 - Economic Statistics
 - Articles

Full Disclosure Principle

Increase in Reporting Requirements

Reasons:

- Complexity of Business Environment.
- Necessity for Timely Information.
- Accounting as a Control and Monitoring Device.

Full Disclosure Principle

Differential Disclosure

"Big GAAP versus Little GAAP".

FASB takes the position that there should be one set of GAAP.

Notes to the Financial Statements

Notes are the means of amplifying or explaining the items presented in the main body of the statements.

Accounting Policies

Companies should present a statement identifying the accounting policies adopted (Summary of Significant Accounting Policies).

Notes to the Financial Statements

Common Notes

- *Inventory*
- *Property, Plant, and Equipment*
- *Creditor Claims*
- *Equity Holders' Claims*
- *Contingencies and Commitments*
- *Deferred Taxes, Pensions, and Leases*
- *Changes in Accounting Principles*

Disclosure Issues

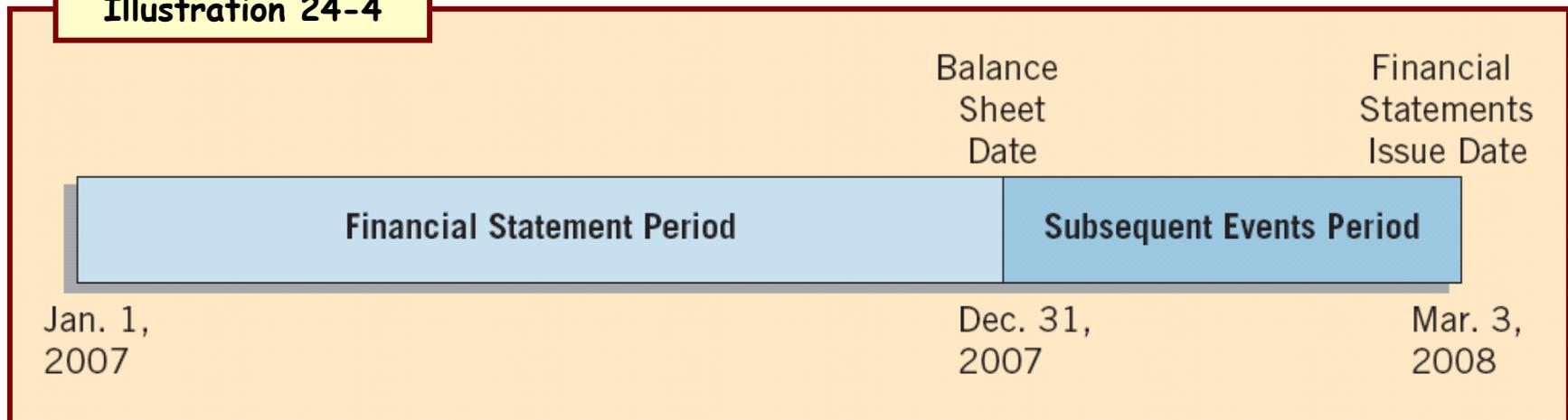
Disclosure of Special Transactions or Events

- Related-party transactions
- Illegal acts

Disclosure Issues

Post-Balance-Sheet Events (Subsequent Events)

Illustration 24-4



1 - Events that provide additional evidence about conditions that existed at the balance sheet date.

2 - Events that provide evidence about conditions that did not exist at the balance sheet date.

Disclosure Issues

Reporting for Diversified Companies

Investors and investment analysts income statement, balance sheet, and cash flow information on the **individual segments** that compose the total income figure.

Disclosure Issues

Objective of Reporting Segmented Information

To provide information about the **different types of business activities** in which an enterprise engages and the **different economic environments** in which it operates.

A company can meet objective by providing financial statements segmented based on how the company's operations are managed (**Operating Segment**).

Disclosure Issues

Segmented Information Reported

1. General information about operating segments.
2. Segment profit and loss and related information.
3. Segment assets.
4. Reconciliations.
5. Information about products and services and geographic areas.
6. Major customers.

Disclosure Issues

Interim Reports

Cover periods of less than one year.

Two viewpoints exist:

1. The discrete approach
2. The integral approach

Companies should use the same accounting principles for interim reports that they use for annual reports.

Disclosure Issues

Unique Problems of Interim Reporting

- (1) Advertising and similar costs
- (2) Expenses subject to year-end adjustment
- (3) Income taxes
- (4) Extraordinary items
- (5) Earnings per share
- (6) Seasonality

Auditor's and Management's Reports

Auditor's Report

Standard **unqualified opinion** - auditor expresses the opinion that the financial statements are presented fairly, in all material respects, in conformity with GAAP.

Other opinions:

- Qualified
- Adverse
- Disclaim

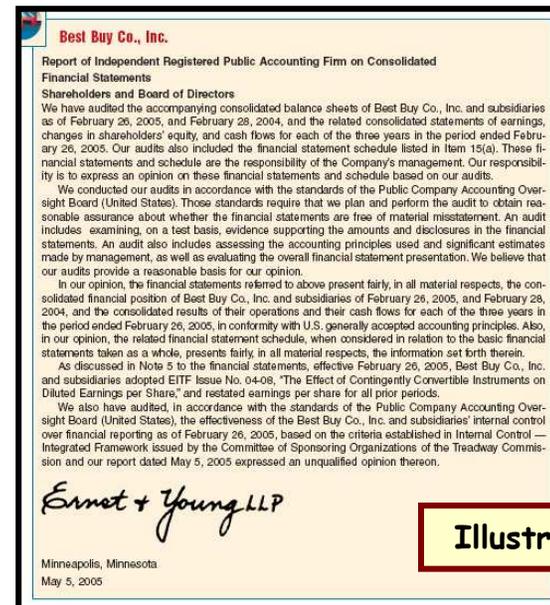


Illustration 24-14

Auditor's and Management's Reports

Management's Report

The SEC mandates inclusion of **management's discussion and analysis (MD&A)**.

Management highlights favorable or unfavorable trends related to liquidity, capital resources, and results of operations.

Auditor's and Management's Reports

Management's Responsibilities for Financial Statements

The Sarbanes-Oxley Act requires the SEC to develop guidelines for *all* publicly traded companies to report on management's responsibilities for, and assessment of, the internal control system.

Current Reporting Issues

Reporting on Financial Forecasts and Projections

Financial forecast is a set of prospective financial statements that present, a company's expected financial position, results of operations, and cash flows.

Financial projections are prospective financial statements that present, given one or more *hypothetical assumptions*, an entity's expected financial position, results of operations, and cash flows. **SEC Safe Harbor Rule**

Current Reporting Issues

Fraudulent Financial Reporting

Intentional or reckless conduct, whether through act or omission, that results in materially misleading financial statements.

The Sarbanes-Oxley Act has numerous provisions intended to help prevent fraudulent financial reporting.

Copyright

Copyright © 2007 John Wiley & Sons, Inc. All rights reserved. Reproduction or translation of this work beyond that permitted in Section 117 of the 1976 United States Copyright Act without the express written permission of the copyright owner is unlawful. Request for further information should be addressed to the Permissions Department, John Wiley & Sons, Inc. The purchaser may make back-up copies for his/her own use only and not for distribution or resale. The Publisher assumes no responsibility for errors, omissions, or damages, caused by the use of these programs or from the use of the information contained herein.