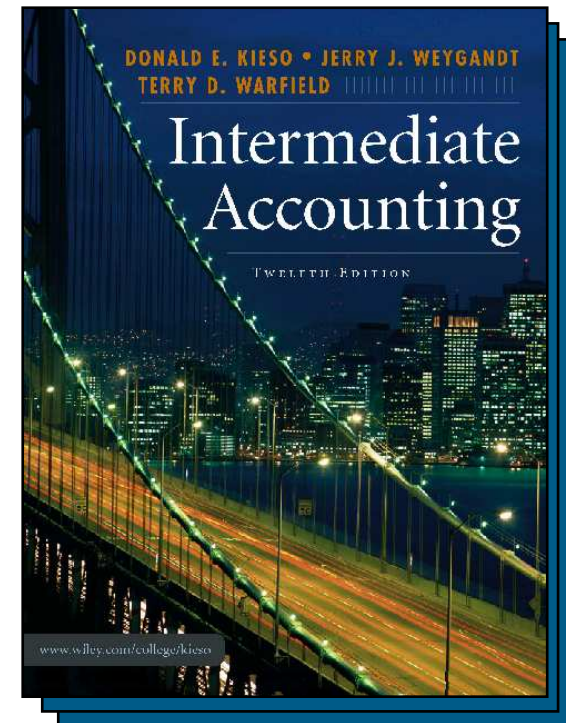


# *Financial Accounting and Accounting Standards*

## Chapter 1

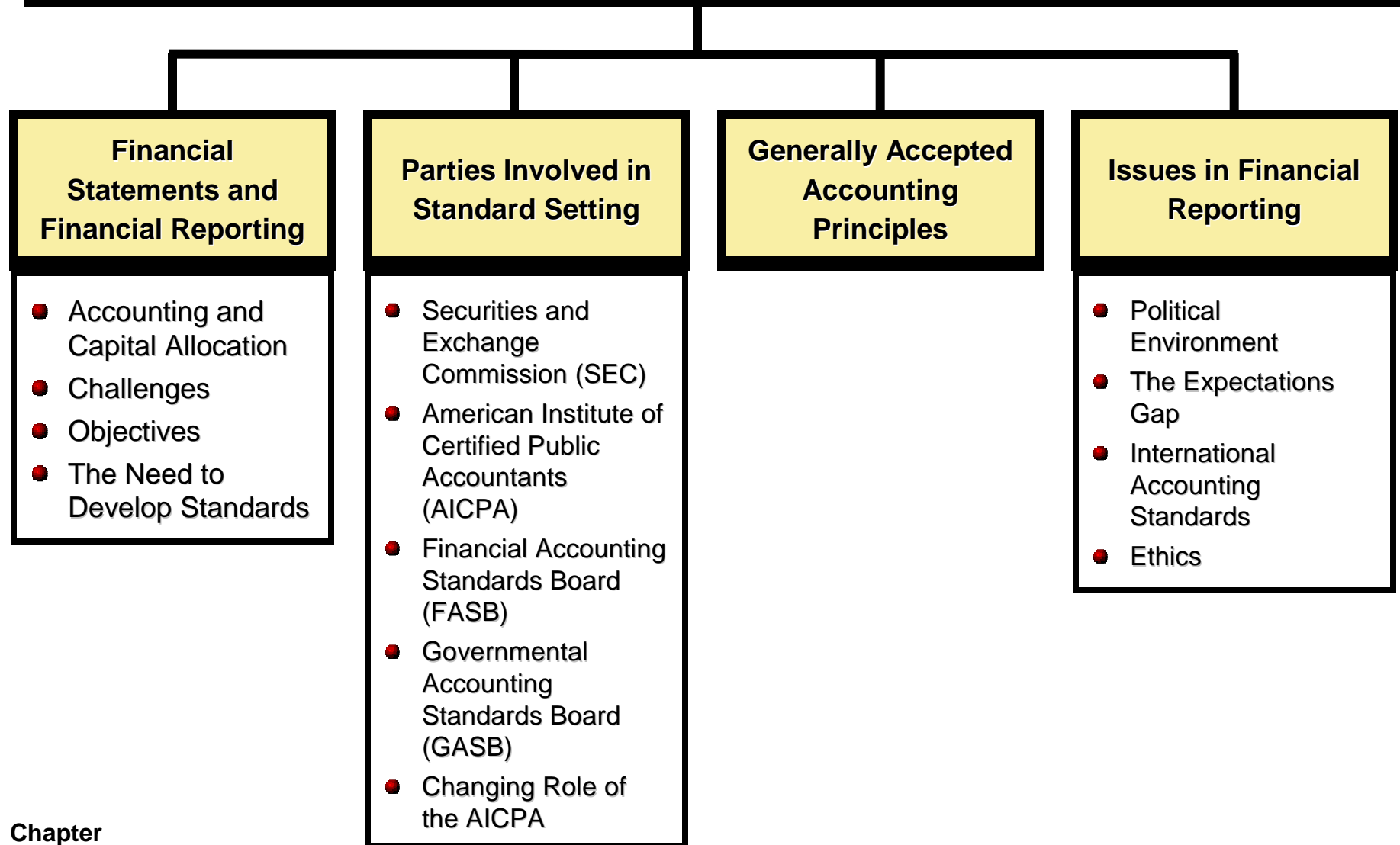
Intermediate Accounting,  
12th Edition  
Kieso, Weygandt, and Warfield



# *Chapter 1 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. Describe some of the challenges facing accounting.
4. List the objectives of financial reporting.
5. Explain the need for accounting standards.
6. Identify the major policy-setting bodies and their role in the standard-setting process.
7. Explain the meaning of generally accepted accounting principles.
8. Describe the impact of user groups on the standard-setting process.
9. Understand issues related to ethics and financial accounting.

# ***Accounting Standards and Financial Reporting***

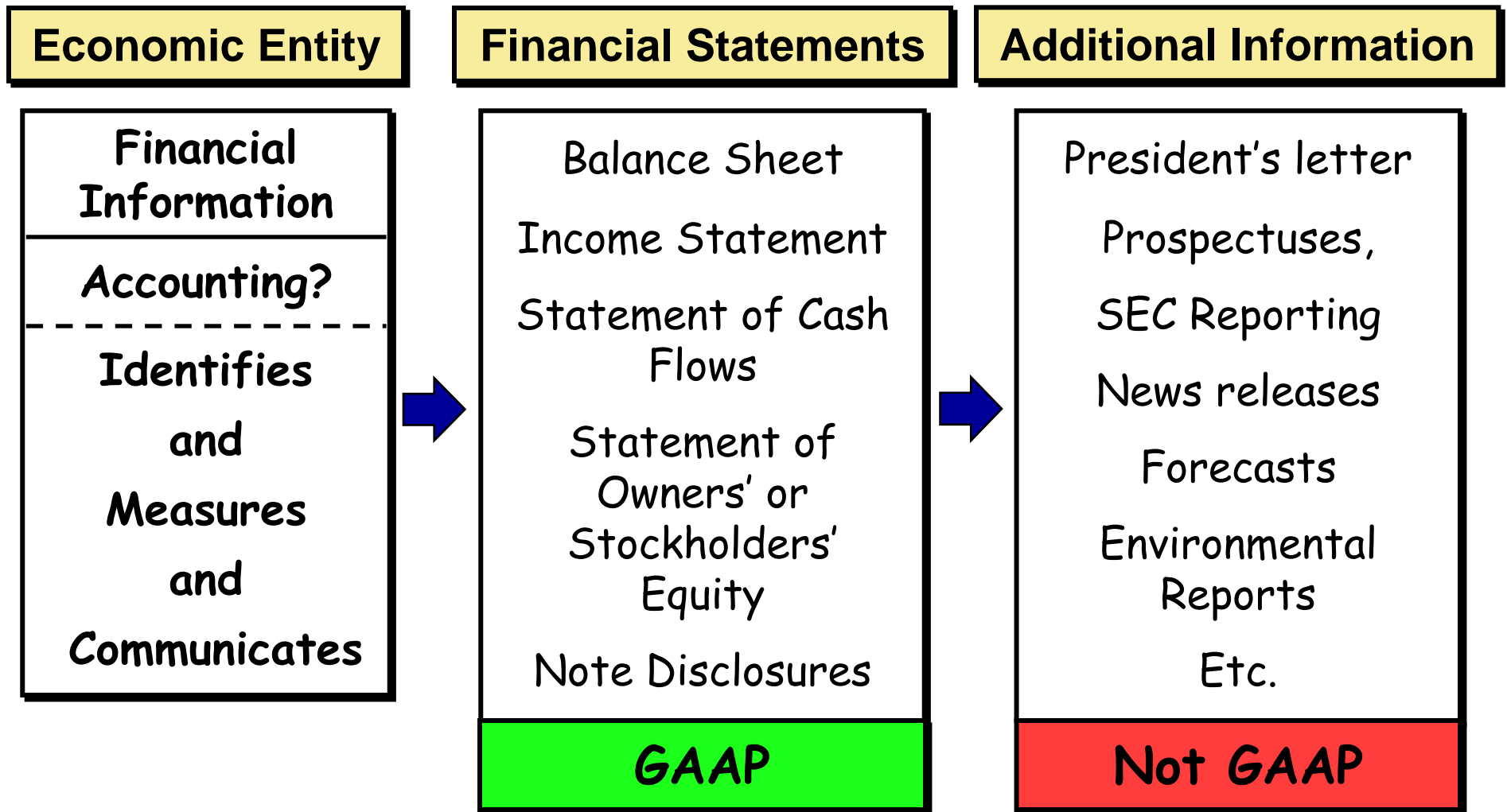


# *Characteristics of Accounting*

Essential characteristics of accounting are:

- (1) the **identification, measurement, and communication** of financial information about
- (2) economic entities to
- (3) interested parties.

# Characteristics of Accounting



# Characteristics of Accounting

## Review

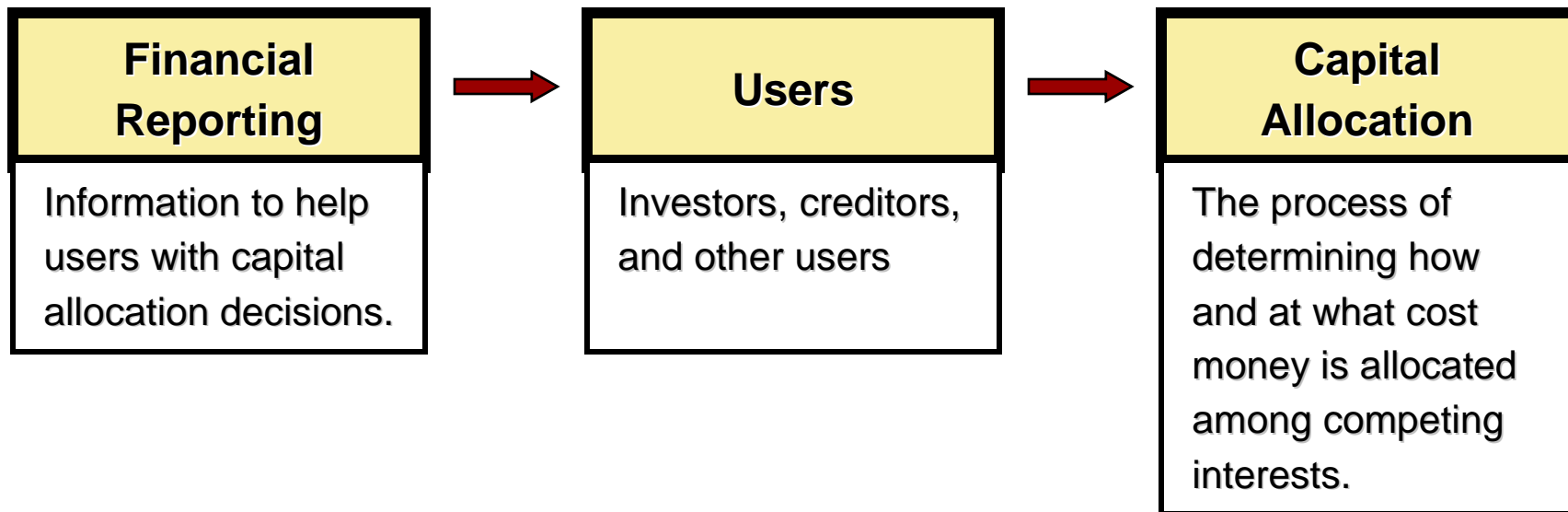
What is the purpose of information presented in notes to the financial statements?

- a. To provide disclosure required by generally accepted accounting principles.
- b. To correct improper presentation in the financial statements.
- c. To provide recognition of amounts not included in the totals of the financial statements.
- d. To present management's responses to auditor comments.

# Accounting and Capital Allocation

Resources are **limited**. Efficient use of resources often determines whether a business thrives.

Illustration 1-1 Capital Allocation Process



# *Accounting and Capital Allocation*

## **Review**

An effective process of capital allocation is critical to a healthy economy, which

- a. promotes productivity.
- b. encourages innovation.
- c. provides an efficient and liquid market for buying and selling securities.
- ☒ d. All of the above.



# *Challenges Facing Financial Accounting*

- Non-financial Measurements
- Forward-looking Information
- Soft Assets
- Timeliness

# *Objectives of Financial Accounting*

Financial reporting should provide information:

- (a) that is useful to present and potential investors and creditors and other users in making rational investment, credit, and similar decisions.
- (b) to help present and potential investors and creditors and other users in assessing the amounts, timing, and uncertainty of prospective cash receipts.
- (c) about the economic resources of an enterprise, the claims to those resources, and the effects of transactions, events, and circumstances that change its resources and claims to those resources.

# *Objectives of Financial Accounting*

## **Review**

All of the following are objectives of financial reporting except to provide information

- a. About enterprise resources, claims to those resources, and changes in them.
- b. That is useful in investment and credit decisions.
- ☒ c. About the management and major shareholders of an enterprise.
- d. That is useful in assessing cash flow prospects.

# *Need to Develop Standards*

Various users  
need financial  
information



## Financial Statements

- Balance Sheet
- Income Statement
- Statement of Stockholders' Equity
- Statement of Cash Flows
- Note Disclosure



The accounting profession  
has attempted to develop a  
set of standards that are  
generally accepted and  
universally practiced.



**Generally Accepted  
Accounting Principles  
(GAAP)**

## *Parties Involved in Standard Setting*

### **Four organizations:**

- Securities and Exchange Commission (SEC)
- American Institute of Certified Public Accountants (AICPA)
- Financial Accounting Standards Board (FASB)
- Government Accounting Standards Board (GASB)

# *Securities and Exchange Commission*

- Established by federal government
- Accounting and reporting for public companies



Securities  
Act of 1933

Securities  
Act of 1934

- Encouraged private standard-setting body
- SEC requires public companies to adhere to GAAP
- SEC Oversight
- Enforcement Authority

# *American Institute of CPAs*

- National professional organization
- Established the following:

## Committee on Accounting Procedures

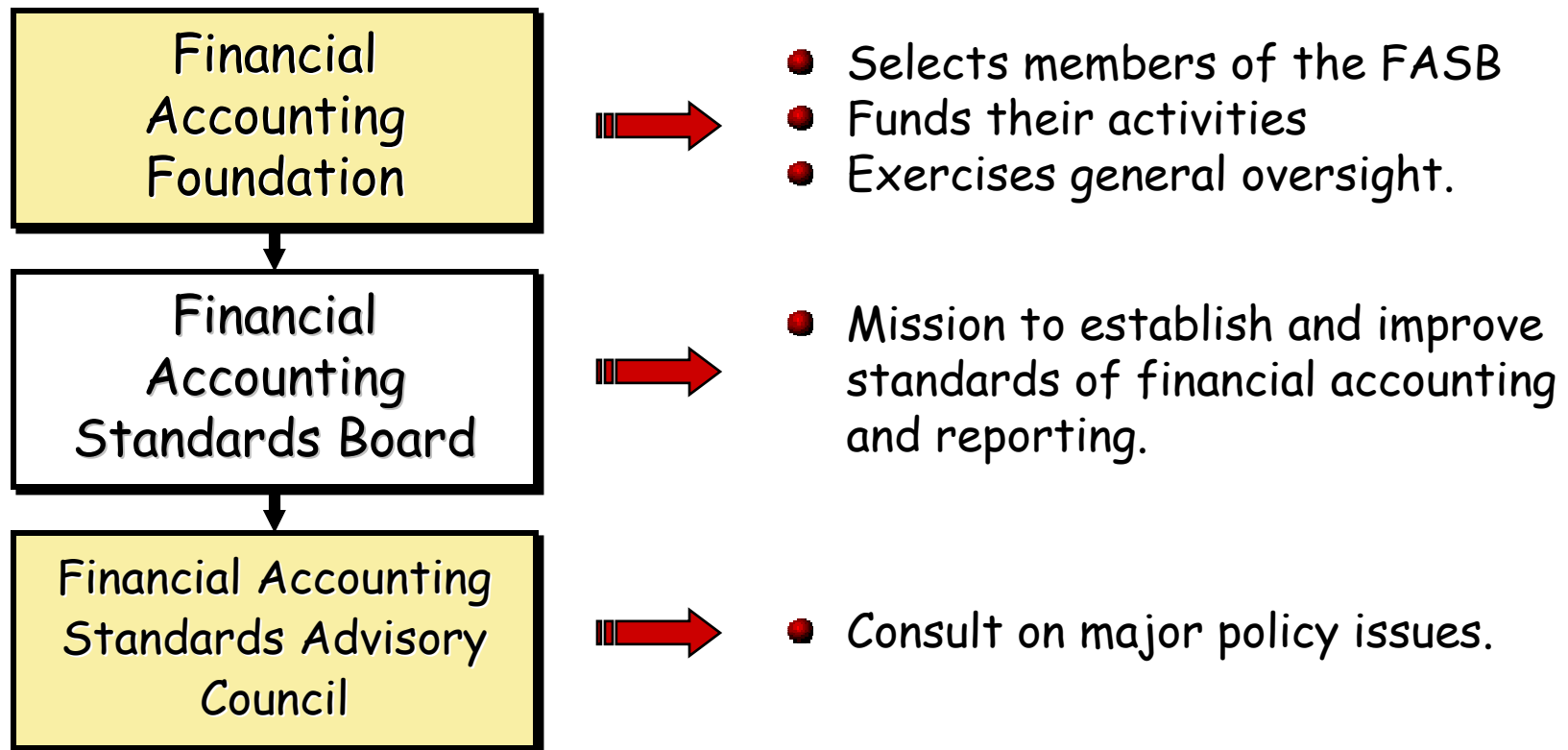
- 1939 to 1959
- Issued 51 Accounting Research Bulletins (ARBs)
- Problem-by-problem approach failed

## Accounting Principles Board

- 1959 to 1973
- Issued 31 Accounting Principle Board Opinions (APBOs)
- Wheat Committee recommendations adopted in 1973

# *Financial Accounting Standards Board*

Wheat Committee's recommendations resulted in the creation of a the **Financial Accounting Standards Board** in 1973.





# *Financial Accounting Standards Board*

Missions is to establish and improve standards of financial accounting and reporting. Differences between FASB and APB include:

- Smaller Membership
- Full-time, Remunerated Membership
- Greater Autonomy
- Increased Independence
- Broader Representation



<http://www.fasb.org/>

# *Financial Accounting Standards Board*

## **Review**

The first step taken in the establishment of a typical FASB statement is

- a. The board conducts research and analysis and a discussion memorandum is issued.
- b. A public hearing on the proposed standard is held.
- c. The board evaluates the research and public response and issues an exposure draft.
- d** Topics are identified and placed on the board's agenda.

# Due Process

FASB relies on two basic premises:

- (1) Responsive to entire economic community
- (2) Operate in full view of the public

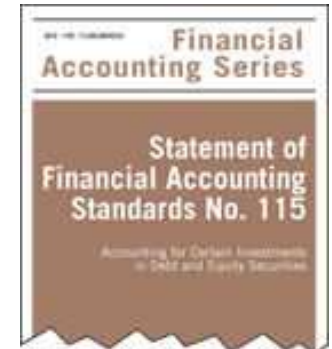
**Step 1** = Topic placed on agenda

**Step 2** = Research conducted and **Discussion Memorandum** issued.

**Step 3** = Public hearing

**Step 4** = Board evaluates research, public response and issues **Exposure Draft**

**Step 5** = Board evaluates responses and issues final **Statement of Financial Accounting Standard**



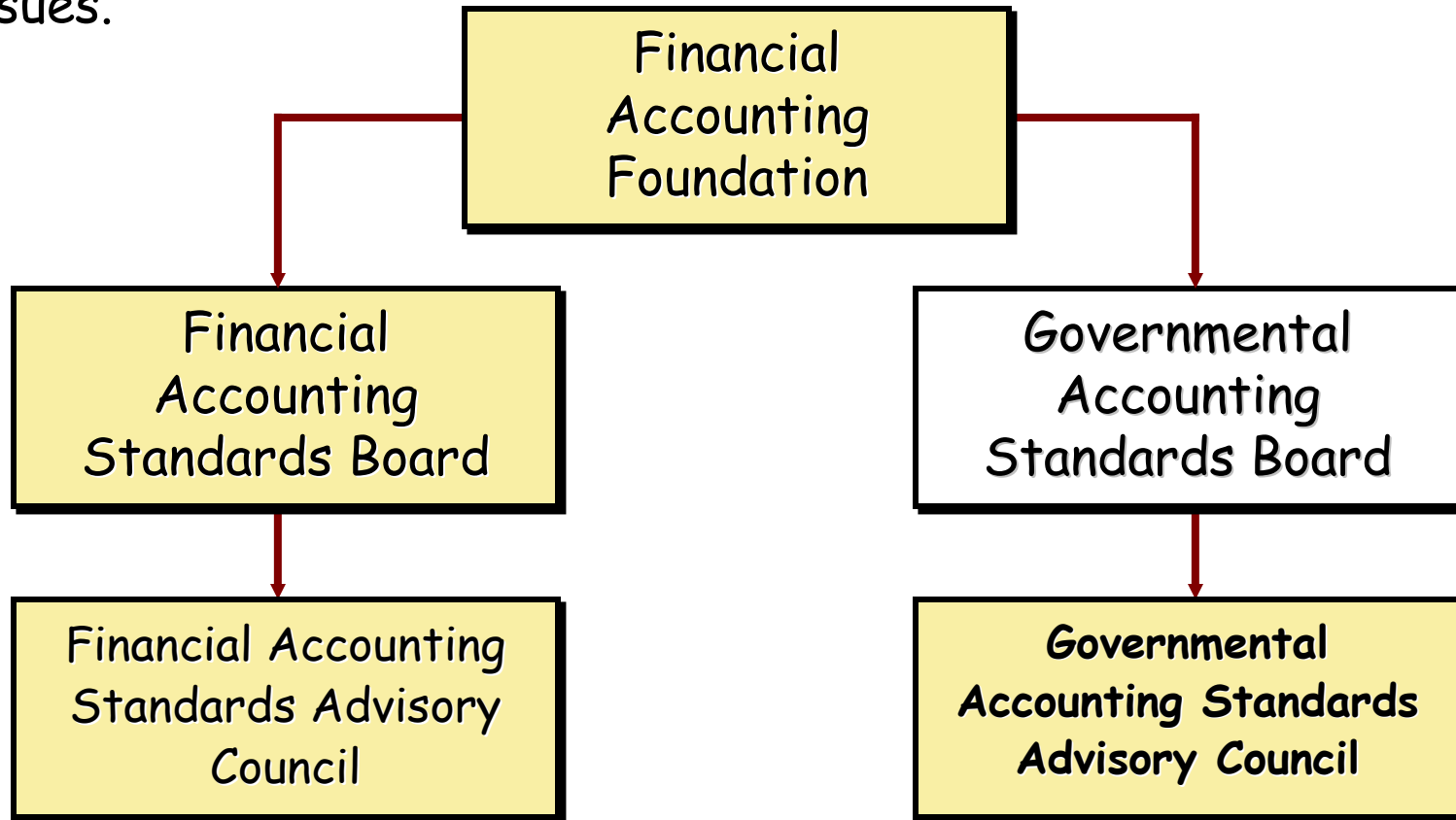
# *Types of Pronouncements*

Issued by the FASB:

- Standards, Interpretations, and Staff Positions.
- Financial Accounting Concepts
- Emerging Issues Task Force Statements

# *Governmental Accounting Standards Board*

Created in 1984 to address state and local governmental reporting issues.



# *Generally Accepted Accounting Principles*

Those principles that have **substantial authoritative support**.

Major sources of GAAP are:

- FASB Standards, Interpretations, and Staff Positions
- APB Opinions
- AICPA Accounting Research Bulletins

# *House of GAAP*

AICPA Accounting  
Interpretations

FASB Implementation  
Guides

Recognized Industry  
Practices

## **Category D (Least Authoritative)**

FASB Emerging Issues Task Force

AICPA AcSEC Practice Bulletins

## **Category C**

FASB Technical  
Bulletins

AICPA Industry Audit  
and Accounting Guides

AICPA Statements of  
Position

## **Category B**

**FASB Statements,  
Interpretations, and  
Staff Positions**

**APB Opinions**

**CAP Accounting  
Research Bulletins**

## **Category A (Most Authoritative)**

# *Generally Accepted Accounting Principles*

## **Review**

Which of the following accounting pronouncements is the most authoritative?

- a. FASB Statement of Financial Accounting Concepts.
- b. FASB Technical Bulletins.
- ☒ c. AICPA Accounting Principles Board Opinion.
- d. AICPA Statement of Position.



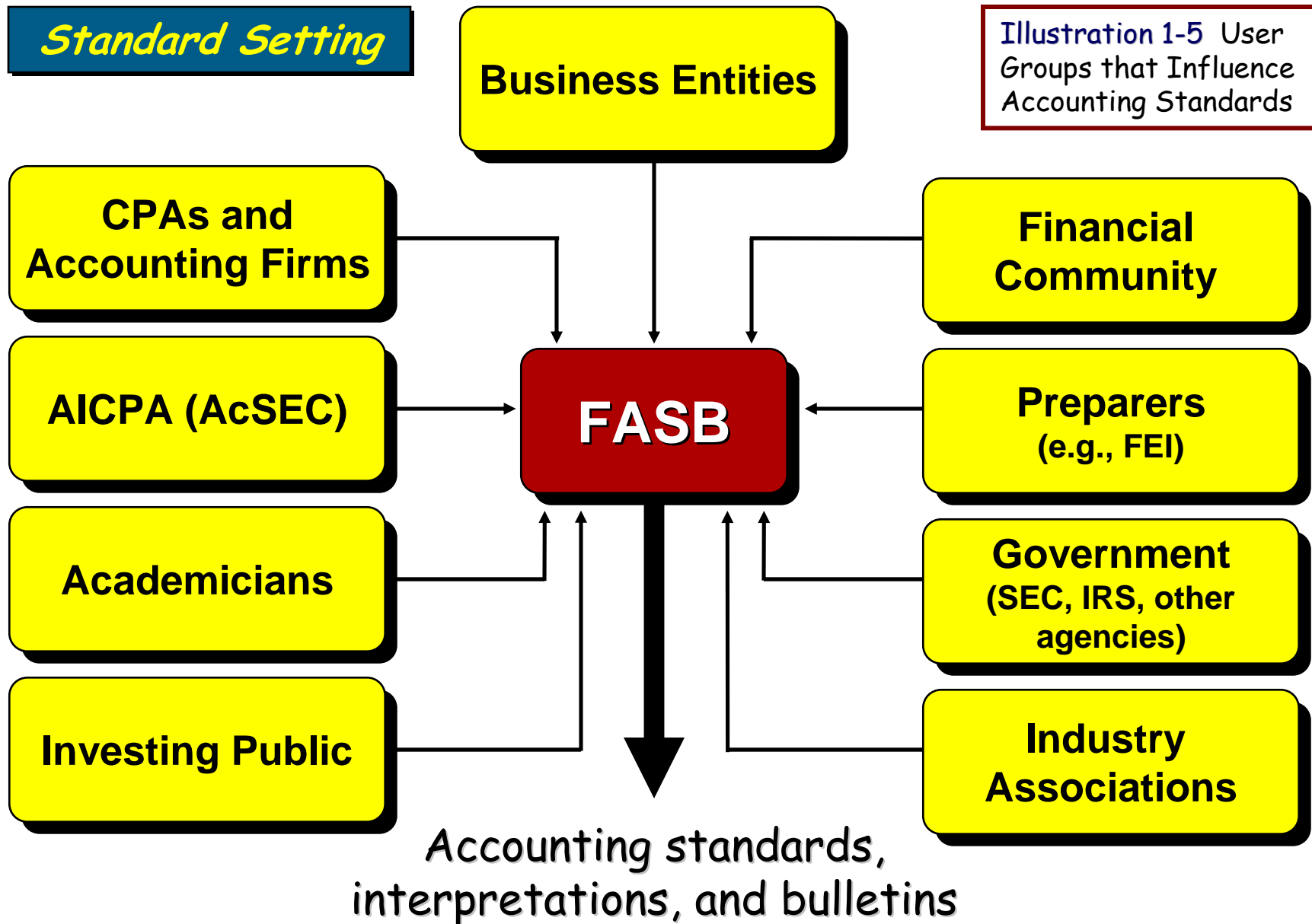
# *Issues in Financial Reporting*

## **Standard Setting in a Political Environment**

Accounting standards are as much a product of political action as they are of careful logic or empirical findings.

## *Standard Setting*

**Illustration 1-5** User Groups that Influence Accounting Standards



## *Issues in Financial Reporting*

### **Review:**

All those who serve on the FASB must be Certified Public Accountants.

**False**

# *Issues in Financial Reporting*

## **Expectation Gap**

What the public thinks accountants should do **vs.** what accountants think they can do.

- Difficult to close
- Sarbanes-Oxley Act (2002)
- Public Company Accounting Oversight Board (PCAOB)

# *Issues in Financial Reporting*

## **International Accounting Standards**

Two sets of standards accepted for international use:

- U.S. GAAP, issued by the FASB
- International Financial Reporting Standards (IFRS), issued by the IASB

FASB and IASB recognize that global markets will best be served if only one set of GAAP is used.

# *Issues in Financial Reporting*

## **Ethics in the Environment of Financial Accounting**

In accounting, we frequently encounter ethical dilemmas.

- GAAP does not always provide an answer
- Doing the right thing is not always easy or obvious

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