

9-2003

## ACCT 615.01: Accounting Theory

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ACCT 615 - Fall 2003

Office hours: W 9-11:45, TR 11-11:30 & 2-3:30  
Also by appointment

NOTE: Office hours may change sometimes

Date	Reading	Assignment
Sept. 2	---	Introduction
4	1(4-12), 3	A. (Accounting Theory) B. (History)
9	4, 2(43-46)	C. (Regulation)
11	5(130-149)*	D. (GAAP)
16	7(195-220, 223-225)	E. (Conceptual Framework)
18	APB #22, 8**, 6(183-190)	F. (Disclosure) G. (Useful Information)
23	9***	H. (Uniformity and Disclosure)
25	11****, 10(316-320)	I. (Income Statement)
30	---	CATCHUP - CLASS WILL BE HELD
Oct. 2	EXAM I	Individual test and group test (DOUBLE CLASS)
7	FAS #130, FAS #7	J. (Comprehensive Income) K. (Dev. Stage Cos.)
9	<b>D &amp; B Due in Beed's office by classtime – review Exam I</b>	
14	10(345-349, 356-359)	L. (Stockholder's Equity)
16	---	CATCHUP – CLASS WILL BE HELD
21	13****, Appendix 1-A*****	M. (Price Changes)
23	---	CATCHUP – CLASS WILL BE HELD
28	16*****	N. (Leases)
30	---	CATCHUP – CLASS WILL BE HELD
Nov. 4	HOLIDAY	---
6	FAS #131, FAS #34	O. (Segment Reporting) P. (Interest Capitalization)
11	EXAM II	Individual test and group test (DOUBLE CLASS)
13	<b>No Class - Work on finalizing your term papers</b>	
18	<b>Homework Qsts and Term Papers Due (with copies for all) – review Exam II</b>	
20	<b>No class – work on PowerPoint Presentations</b>	
25	Packet Material	Q. (Derivatives)
27	HOLIDAY	---
Dec. 2	<b>No Class - Work on PowerPoint Presentations</b>	
4	Two Papers (HO Homework)	R. (Enron, etc.) S. (Restructure of Prof.)
Dec. 9	Three Papers (HO Hmwrk)	T. (Int'l Harm.) U. (Env. Liab.) V. (Liability/Stock)
11	Two Papers (HO Homework)	W. (Stock Options I) X. (Stock Options II)
Final Week	EXAM III (Tuesday, December 16 from 10:10-11:30)	

\* Do pay attention to the equations at the end of this chapter. They are theoretical equations, not mathematical equations.

\*\* SKIP – section from bottom of 242 to last section on 248

\*\*\* SKIP – from Segments on 295 to Quarterly Info on 300

\*\*\*\* SKIP - section on Future Events on 379-382 and Specialized Subjects on 391-399.

\*\*\*\*\* SKIP - section on Income Measurement Systems on 463-476 and Special Problems on 479-486 .

\*\*\*\*\* Ignore the exhibits per se. Concentrate on the concepts of each attribute being discussed.

\*\*\*\*\* SKIP – section on evolution on 583-SFAS No. 13 on 585 and APB #7 and #27 on 590-591

- Appendices are not included in assignments unless so indicated.

**School of Business Mission Statement:** The faculty and staff of The School of Business Administration at The University of Montana-Missoula are committed to excellence in innovative experiential learning and professional growth through research and service.

**HOMEWORK:**

- Homework points are based on homework turned in and credit received as a percent of total points received on all homework collected. For example, if you get credit for 80% of the homework, you will get 80 points (100 X 80%.) No late homework will be accepted except for unusual circumstances that I determine are appropriate on an individual basis. **HOMEWORK MUST BE TYPED AND SPELLCHECKED.** It can be single-spaced or double-spaced.
- I highly recommend that you actually type out answers to the extra credit questions, but do not turn them in since I will not be grading them.
- On Nov. 18, your group will make available a copy of your term paper for each member of the class and for Beed. As a group, you will compose and hand out four homework questions covering your paper. They are also due on Nov. 18. The correct answers and where they could be found in your paper will be compiled on a separate sheet and given to Beed to be used to grade the homework handed in by the class. These questions will be graded for quality and material coverage. All group members will receive the same grade for these questions. Homework answers will not be shared with class members in other groups. **A GROUP DOES NOT DO THEIR OWN HOMEWORK FOR THEIR OWN TOPIC.**
- Group papers will be used as homework assignments for the last three class days. Group term papers will also be the basis for the professional presentations.

**POINTS:** Your grade will consist mainly of the following points:

EXAM I (individual and group exam)	120	There are no makeup exams due to the group nature of the exams.
EXAM II (individual and group exam)	120	
EXAM III (individual exam only)	100	
HOMEWORK	100	
DESC. AND BIBLIOG.	20	
TERM PAPER	100	
Personal Opinion - term paper	10	
PEER GROUP EVALUATION (D & B)	10 (By individuals)	
PEER GROUP EVAL (PAPER & PRESENTATION)	10 (By individuals)	
5 GROUP HOMEWORK QSTS & ANSWERS	20	
Class Presentation Ranking and Evaluation	50 (By classmates and guests)	
Class Paper Ranking	10 (By individuals)	
Total points possible	670	

**There is no such thing as a late description and bibliography or a late term paper.**

Whatever your group has done by the required deadline on each is what I will grade. Substantial points are lost if either is turned in incomplete, however. Your group is responsible for these assignments as a group and no excuses regarding "whose fault it is" if the assignment is late will be accepted. A term paper will not be accepted if the description and bibliography was not turned in by the required deadline.

**ASSIGNMENT MATERIAL:**

Wolk, Harry I., Michael G. Tearney, and James L. Dodd (2003), *Accounting Theory*, (Sixth Edition, South-Western Publishing Company)

The following materials may be found in Beed's office:

- APB #22 and FAS #7, 34, 130, 131
- Intermediate Text material on derivatives

**Group Presentation Ground Rules:**

- You will use PowerPoint to present your material.
- You will dress in professional attire.
- The presentation must cover the material in your term paper, but you may add other material also.
- Each person must give approximately an equal part of the presentation, but it must flow. It must be evident that you built and worked on the presentation together and that each person did not just take one part and then the whole was pasted together. Each of you needs to work on building the PowerPoint – this 'skill' is expected in 'real life.' All of you will use it during your part of the presentation. Someone else will not 'run' it for you. You are ready to present when it is clear that all of you could give any part of the presentation. In other words, you are not prepared only to give 'your' small part of the talk.
- Practice is a must.
- Presentations need to be at least 30-60 minutes in length. You may not exceed 60 minutes. Make sure you are presenting new material as you progress – do not be repetitive.
- Questions and answers will follow. All of you will answer questions and I will expect all of you to be able to answer questions over all of the talk, not just the section you presented. You must know the material that everyone presented. It is a group paper and a group presentation.
- Fancy PowerPoint items (such as shooting stars, music, info entering from all directions) is O.K. but is not required. Remember, the medium must be used to increase the quality of the material. Fancy presentation with little or no content is a bomb.
- Since other faculty and accounting professionals from the area will be invited to all presentations, you must begin the presentation by introducing yourselves.
- Each team will handout a formal Reference List to each outside attendee after the presentation.
  - Other handout material is acceptable, but not required. And, again, it should be clear that it improves the presentation and isn't just wasted paper.
- All in attendance, 615 students and visitors, will complete an evaluation form after each presentation.

## ASSIGNMENTS

### A. (Chapter 1)

1. When you registered for this class, what did you think the material in the class would cover? In other words, what did you envision Accounting Theory to be?
2. In your own words, define what objectivity means in accounting.

#### **EXTRA**

3. Accounting policies are derived from three main sources. Name and briefly describe the role each source plays in the policy-making process.

### B. (Chapter 3)

BOOK QUESTIONS: 9, 19

1. Why was there a lack of uniformity in accounting practices between companies before the 1920s?
2. Who were the main users of financial reports before the 1920s, what types of information did they want, and why did they want it?
3. Since the SEC first allowed the accounting profession to put out accounting rules, how many groups have done this? Name the groups and the time periods during which each promulgated rules. Name at least one reason why each of the first two groups was dissolved and replaced by another group.

**EXTRA** – Book Question 5, 7, 15

4. What part did the Wheat Committee play in changing accounting rule-making?
5. What are some of the current complaints about the FASB?
6. What is the EITF and what role does it play in accounting rule-making?

### C. (Chapter 4 and Part of Chapter 2)

BOOK QUESTIONS from Chapter 4: 1, 2, 8, 23

1. What is the most surprising thing you learned in this chapter? Why was it surprising to you?
2. In your own words, what is agency theory and how does it relate to financial accounting?

**EXTRA** – Book Questions from Chapter 4: 7, 24

3. Will improved financial reporting eliminate fraud and business failure? Why or why not?
4. In general, what types of accounting policies do auditors oppose? Why?

### D. (Chapter 5)

BOOK QUESTION: 19

1. Of all the principles and postulates listed on pages 132-142, which one do you believe is the most useful today? Why? (This is not in the book. Give your own thoughtful answer.)
2. Why is materiality in accounting a hard concept to define and use?
3. When the entity theory (page 144) was first proposed, creditors became worried. Why? (Think about this. The answer is only found indirectly in the book.)
4. What is an interim statement and why have they become popular?

### E. (Chapter 7)

BOOK QUESTION: 2

1. Do the authors of the text seem to believe that economic consequences should be the main characteristic the FASB considers when setting standards? If so, why? If not, what is the main characteristic?
2. Do you believe that the FASB should make economic consequences play a major role in standard setting? Why?
3. Reread the information in Chapter 4 regarding due process. Compare the concept of due process with the concept of neutrality as they relate to accounting policy setting. (Do not just define each concept. Compare them to each other as they relate to accounting policy setting.)
4. Briefly summarize the main idea behind each of the six concepts of the Conceptual Framework Project.

**(continued on next page)**

5. Do you believe that the FASB relies more heavily on relevance or reliability in setting standards? Give your opinion, but carefully back it up with at least two examples from intermediate accounting to justify your opinion.

**EXTRA**

Book Question 3, 7

6. Briefly define the three aspects of relevance.
7. Briefly define the three aspects of reliability.

**F. (APB #22)**

1. Why did the APB put out this ruling?
2. What information in general did the APB require be disclosed? (Do not give a list of specifics.)
3. Where exactly should the information be disclosed?

**G. (Parts of Chapter 8 and Chapter 6)**

BOOK QUESTION FROM Chapter 8: 11

1. Why does the accounting profession publish one type of financial statement for everyone when there are a lot of user groups other than investors?
2. What is the efficient markets hypothesis and what are its three forms? How does this relate to accounting?
3. According to the text, is cash flow or earnings a better predictor of future cash flows?

**EXTRA**

Book Questions from Chapter 8: 1, 2

4. What is portfolio theory? Why might this theory be helpful?

**H. (Chapter 9)**

BOOK QUESTION 10

1. What is a "safe harbor" provision and why would the accounting profession like more of these provisions?
2. What is competitive disadvantage with regard to financial statements? How does it relate to the disclosure concept?
3. What is the difference between finite uniformity, rigid uniformity, and flexibility? Give an example of each.
4. What is a relevant circumstance in financial accounting? Define and give an example. When you give an example, explain HOW it is an example.

**EXTRA**

BOOK QUESTIONS: 7, 17, 22

5. What is information overload in accounting? Why can it be a problem?

**I. (Chapter 11 and Part of Chapter 10)**

1. Differentiate between the asset/liability vs. revenue/expense approach of measuring income. (Do not just define each. What is the difference?) Which has been the traditional approach?
2. What are the three hierarchies of the matching principle and how is each applied or used in accounting?
3. Differentiate between the current operating vs. all-inclusive income concepts. (Do not just define each.) Which method is used today?
4. The following categories of items are found on financial statements. Put each one in the proper order in which it would be found on the income statement. If a listed item is not found on the income statement, give a detailed explanation regarding where it would be found on a set of financial statements. Assume a multiple-step format. You may need to use your intermediate book to help you.

Change in principle	Discontinued operations	Prior period adjustment
Earnings per share	Extraordinary items	"Other" revenues and expenses
Operating cash flow	Operating income	Dividends

(continued on next page)

**EXTRA**

5. What is a summary indicator in accounting? Give four examples of a summary indicator.
6. What is income smoothing? Why might management want to smooth income?
7. Differentiate between articulated and nonarticulated financial statements.

**J. (FAS #130)**

1. What is the purpose of reporting comprehensive income?
2. Under existing accounting standards what items will be included in "other comprehensive income?"
3. FASB allowed three formats for reporting comprehensive income. What are they? Which is the one the FASB likes the least?
4. How should tax effects be displayed according to this standard?

**K. (FAS #7)**

1. Define development stage company.
2. Development stage companies wanted different reporting standards for themselves. Why do you think they wanted different standards? (The answer is not directly in the reading. Give a good answer of your own.)
3. Did the FASB allow a different set of rules for development stage companies? Give a reason for your answer.

**EXTRA**

4. List several activities in which development stage companies are involved.

**L. (Chapter 10)**

**BOOK QUESTION: 18**

1. According to the book, there are three components of owners' equity. Name and describe each.
2. Technically, the recipients of a stock dividend do not receive anything of value. Why not? (Carefully explain what you mean in your answer. Do not just give some definitions.)
3. Define operating cycle and then indicate how it is used for classification purposes on the balance sheet.
4. What are some of the most common reasons for Treasury Stock existing today?

**EXTRA**

5. What is the difference between shares issued and shares outstanding?

**I highly recommend that you do the entries below!!**

Give the proper entries for each of the following. The entries are not in your book. Honestly see how you do before looking them up. Test yourself. Hint: You covered these entries in principles and intermediate accounting.

**In all cases, assume the par value of the stock is \$100 and the stock originally sold for \$110.**

**6-8 each require two entries.**

6. Declare and pay a \$40 cash dividend.
7. Declare and pay a small stock dividend. Assume market value is \$130.
8. Declare and pay a large stock dividend. Assume market value is \$130.

**For 9-11, use the single-transaction approach. (Cost method.)**

9. Buy treasury stock at \$116.
10. Sell the treasury stock for \$123.
11. Sell the treasury stock for \$112.

**For 12-15, use the two-transaction approach. (Par value method.)**

12. Sell the stock originally.
13. Buy treasury stock at \$112.
14. Buy treasury stock at \$104.
15. Sell the treasury stock at \$115.

M. (Chapter 13 and Appendix 1-A)

BOOK QUESTIONS IN APPENDIX 1-A: 13, 14

BOOK QUESTIONS IN Chapter 13: 3, 11 (Compute the gains or losses. Some are losses.)

1. Distinguish between a **purchasing power** gain/loss vs. a **holding** gain/loss. (Do not give an example. Answer the question.)
2. Distinguish between a **monetary holding** gain/loss vs. a **real holding** gain/loss. (Do not give an example. Answer the question.)
3. Do you believe that you would find it easier to explain price-level adjusted financial statements or current value financial statements to your non-business friends? Give a thoughtful, reasonable answer.
4. Forget the book information. In your opinion, do you believe financial statements should continue to use historical cost or switch to current value? Give a thoughtful explanation for your answer.

**EXTRA**

5. Three reasons were given in support of historical cost. Give them.
6. What is the difference between a specific price index and a general price index?
7. The book states that an asset should be sold if  $PV < NRV$ . Why is that true?

N. (Chapter 16)

BOOK QUESTIONS: 6

1. The concept of substance over form is quite apparent in the lease standard. How? Be specific.
2. According to FAS #13, what is the one, overriding concept that the FASB used to determine whether a lease should be capitalized? (Do not give any of the four capitalization criteria.)
3. What is the basic difference between a sales-type lease and a direct financing lease? (Do not give examples.)
4. Land leases have slightly different rules to follow than do other lease assets. What is the difference and why is land treated differently?
5. Sometimes a leased asset is amortized/depreciated over its useful life and sometimes over the lease term. How is the proper method determined?
6. The FASB required lessees to use the lower of two prescribed interest rates to calculate the present value of the minimum lease payments to record the entry for the asset and the liability in a capital lease. What did that rule do to the amount to be recorded? (This answer is not directly given in the book. Think about it and then answer.)

**EXTRA**

Book Questions 7, 8, 11, 13

7. What is off-balance sheet financing with regard to leases?
8. What are lease executory costs and how are they accounted for in a capital lease?
9. What is included in minimum lease payments in a capital lease?

O. (FAS #131)

1. Why did the FASB put out this standard?
2. Before the quantitative threshold tests can be run, a company has to know how many segments it has in order to run tests on them. How are the number of segments originally determined (even before any test is run?)
3. After a company determines the number of significant segments it has according to the FASB guidelines, it must then apply upper and lower-limit guidelines to determine if it has too few or too many segments. What are these upper and lower-limit guidelines and how are they applied?
4. Many companies were severely opposed to the first standard on this topic (FAS #14.) Why do you think this was the case? (Think of a good answer of your own.)

**EXTRA**

5. In general, what types of qualitative information must a company report about its significant segments?

(continued on next page)



6. How should companies report segments that are determined not to be significant according to the FASB guidelines?
7. What is required on interim reports?
8. How should a company handle a segment that has never met any quantitative thresholds in previous years, but does this year?

P. (FAS #34)

1. What is the limit on how much interest can be capitalized in one period?
2. Capitalization of interest can continue only while three conditions are being met. What are the three conditions?
3. The SEC seemed to be against capitalization of interest. But, after this standard came out, the SEC dropped its previous ruling. Why do you think the SEC did this? Is it because the FASB standard followed the SEC ruling? (The answer is not in the reading or in any of your other textbooks. Give a good, thoughtful answer of your own.)
4. According to GAAP, interest has always been accrued as incurred and was not capitalized. Why did the idea of capitalizing interest come up? (The answer is in the standard here and there, but think about this and give some logical reason of your own.)

**EXTRA**

5. What does it mean to "capitalize" an expense? (The answer is not in the reading. You know this, but if you can't remember, look it up.)
6. If interest can be capitalized, what rate should be used?

Q. (Packet Material on Derivatives)

1. What is a derivative?
2. Why did derivatives use to have off balance sheet risk?
3. What is a hedge? Briefly define the two types of hedging activities.
4. What is a notional amount with regard to derivatives?

**EXTRA**

5. There are four types of risk that derivatives can help manage. Name and summarize each. (Do not just directly copy out of the article.)
6. Name and briefly summarize the four most common types of derivatives.

For topics R-X, the homework will be the questions handed out with the term papers.

## TERM PAPER TOPICS

1. International Standard Harmonization
2. Environmental Liabilities
3. Stock Option Accounting I - from APB #25 to FAS #123
4. Stock Option Accounting II - since FAS #123 (including restricted stock, repriced stock, etc.)
5. Hybrids – Stock or Liability – Debt or Equity? New Controversy and Standard
6. Arthur Andersen, WorldCom, Enron, Tyco – What Accounting Rules were Broken and What Was the Result for the Company and the Executives?
7. Restructure of the Profession – from the Demise of Arthur Andersen to PCOAB and Beyond

Cover the following in your paper:

- History
- Problem and what caused it
- What has been done or is currently being done by the accounting profession with regard to your topic
- Are other groups involved? If so, who, what, and why?
- What is the current status of the topic?
- What are future options or possibilities regarding your topic?

REMINDER: \* Your paper will be read and graded by Beed and the entire class.

The final term paper grade will be based on a combined evaluation.

\* The presentation will be graded based on evaluations of those in attendance.

Rank your group's topic preference in order of preference.

1. \_\_\_\_\_
2. \_\_\_\_\_
3. \_\_\_\_\_

Give group members' names.

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1. Many groups believe that one set of international standards is desired due to the growth of international markets, multinational companies, and international investors and creditors.
2. Environmental liabilities is probably the hottest emerging challenge facing accountants and companies today.
3. Stock options was by far the most controversial issue the FASB dealt with to date. It resulted in a new standard (FAS #123) which did not quite replace the old rule (APB #25.)
4. Stock Options has resurfaced and is still a very controversial topic. Why is it still controversial? Some companies are coming up with creative ways to get out of stock options as an employee incentive.
5. For years the FASB has dealt with the issue of what should be classified as stock vs. what is a liability. Recently FASB released a standard to help address this issue.
6. Exactly what accounting games were these companies and their executives playing? Why did they do what they did? What was the outcome?
7. Since Enron many changes have taken place that have affected the accounting profession. New organizations exist that are supposed to help monitor the profession and other related groups. Groups include stock advisors, SEC, FASB, AICPA and many more.