

Standard Setting Should Remain In the Private Sector

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Standard Setting Should Remain In the Private Sector

Abstract

"In lieu of an abstract, below is the essay's first paragraph.

The Financial Accounting Standards Board (FASB) is the body that establishes accounting standards in the United States. The FASB has a specific operating procedure that it goes through before it will issue a statement for a new standard. During the early stages of this process, a task force is appointed to research a topic of concern and a memorandum is issued to invite discussion. Then there is a public comment period, during which information from and views of interested parties are accepted and reviewed. Some parties that often give input are representatives of CPA firms and interested corporations, security analysts, members of professional accounting associations, and academics. The first public hearings are held to accept oral presentations from these parties. Then the FASB deliberates on its findings in order to issue an exposure draft. More public hearings are held, which enable the FASB to modify the exposure draft if they deem it necessary. The final step in this process is a vote and the issuance of a statement. This process is used so that accounting standards are developed in an efficient manner with due process in a public forum.

Standard Setting Should Remain In the Private Sector

By: Nichole L. Calhoun

The Financial Accounting Standards Board (FASB) is the body that establishes accounting standards in the United States. The FASB has a specific operating procedure that it goes through before it will issue a statement for a new standard. During the early stages of this process, a task force is appointed to research a topic of concern and a memorandum is issued to invite discussion. Then there is a public comment period, during which information from and views of interested parties are accepted and reviewed. Some parties that often give input are representatives of CPA firms and interested corporations, security analysts, members of professional accounting associations, and academics. The first public hearings are held to accept oral presentations from these parties. Then the FASB deliberates on its findings in order to issue an exposure draft. More public hearings are held, which enable the FASB to modify the exposure draft if they deem it necessary. The final step in this process is a vote and the issuance of a statement. This process is used so that accounting standards are developed in an efficient manner with due process in a public forum.

The Financial Accounting Standards Board's (FASB) staff is extremely knowledgeable and has very detailed expertise. The FASB's process allows consideration of all related research on a topic, provided by the FASB's expert staff. The board carefully researches the topic and takes the time to find out what aspects of a standard are most important to the interested parties, so that the proposed standard can be reviewed and improved. It doesn't rule out a standard if there seems to be a lot of opposition. Without the knowledgeable staff that the FASB has, it would be difficult to successfully accomplish this task.

The process also incorporates the views of the interested parties. Accounting standards are part of a broader social system.¹ They affect the whole economy (particularly the private sector). Therefore, these are the people that can predict the effects of new standards most accurately. Through the input of various companies and individuals, the standard is revised until it becomes acceptable and appropriate. With their input, it is likely that the outcome will be a superior and more suitable standard. This is one reason why accounting standard setting should remain in the private sector.

Another reason why the government should not take over the responsibility of standard setting is that the government is more susceptible to political influence. Political influence often causes manipulation of the governing body. Years ago, the FASB proposed that companies recognize the cost of executive options. Corporate lobbyists steamrolled Congress and forced the FASB to retreat.² If the lobbyists can put enough pressure on Congress, forcing Congress to make the FASB back down, then imagine how they would be able to directly influence a government body that was actually making the standards. The field of Accounting is presently regarded with much integrity. If politics became involved, this integrity would be doubted at the very least and, at the most, would disappear.³

It is a fact that outside parties can put more pressure on the government than they can on a private body such as the FASB. For example, if a company has been a substantial supporter of a legislator, the legislator is more likely to take into account that company's opinion. The FASB doesn't "owe" any one company anything. When the FASB is making the standards there is no one company that has any more influence than another; all parties have equal opportunity to voice their opinion.

One chief executive complained that he knew how to lobby Congress but he couldn't figure out how to lobby the FASB.⁴ This demonstrates that the FASB is not as easily influenced. The fact that you can't lobby the FASB should make people feel that the process for setting standards is credible. There is nothing that states that the board has to accept the views of even the majority of its constituents, much less the parties that try to influence them. The mission statement of the FASB states that "the ultimate determinant of concepts and statements ... must be the FASB's judgment, based on research, public input, and careful deliberation, about the usefulness of the resulting information." The decision is not based on what the majority wants.

There are many organizations and individuals that believe that the standard setting process should remain in the private sector. In an editorial in *Business Week* it was stated that the FASB "ought to be free to do its job: to make rules based on public debate rather than arm-twisting by such powerful groups as the Business Roundtable." The individual that wrote this definitely believes that the powerful groups should not have influence on the standard setting body. If the SEC were to take over the responsibility, this would most likely be unavoidable.

The Financial Accounting Foundation (FAF) funds, oversees, and selects members of the FASB and GASB (Government Accounting Standards Board) and their advisory councils. The FAF strongly supports standard setting in the private sector for financial reporting. A letter that the FAF wrote states that they believe that FASB has

developed financial accounting and reporting standards that are widely recognized as the best in the world. Those standards contribute, in large measure, to the efficient functioning of the capital markets and the strength of our economy because of the effective allocation of resources based on credible and understandable financial information.⁵

FASB has improved the field of financial accounting and will continue to do so if it remains in the public sector. Also in this letter, the FAF discusses the actions of the Wheat Committee, which was the committee that originally recommended the present structure for standard setting. The committee worked for 12 months, including holding a two-day public hearing, on finding the best process for setting standards. During this 12-month period, it considered many alternative structures. The committee even considered increased involvement by the Securities and Exchange Commission (the SEC now oversees the FASB in their process). However, the committee concluded that those alternatives would not be in the public's best interest and would not enhance the financial reporting process. They recommended a private sector structure that involved participation by knowledgeable individuals with a diverse range of skill and perspectives. This is exactly what the FASB is and exactly why it is successful.

The SEC has been highly regarded by all as an outstanding regulatory agency, however, faced with a topic as complex and slippery as financial accounting standards, (before a private sector board was established) the regulators weren't sure what to do.⁶ This is why another more specialized agency became necessary and was formed. If the SEC were to try to take over the responsibility now, it would have the same difficulty.

The SEC does not have the advantage of having the highest levels of technical expertise and experience that the FASB has available to them. Therefore, they would not be able to produce standards that were as well researched. They would not have as much input from outside parties as the FASB does; this would decrease the ease of acceptance. The quality of the standards along with their general acceptance would be sacrificed if the SEC were to take over the duty of standard setting.

The reason why some large corporations want to have the SEC take over the responsibility of standard setting is because they have strongly disapproved of some standards that the FASB has been issuing or is considering issuing. A few standards that are not popular with a few companies is a small price to pay for upholding the integrity and ethics of the accounting profession. The many advantages of keeping this process outweigh these small and intermittent discontentments.

The FASB was originally "designed to broaden participation in the standard-setting process, and therefore increase acceptance."⁷ Since these standards are made to govern the behavior of accountants, the accountants should accept the standards. The best way to ensure acceptance of the standards is to enable the affected parties to submit their input. Throughout its years as the standard setting body, the FASB has used their system to produce quality standards that are accepted by the accounting community at large.

There is no reason why the government should replace it and there is no evidence that the government could do a better job. As a matter of fact, there are many reasons why it can be concurred that the government will do a poorer job. There is the fact that the government is more easily influenced, has repeatedly shown a lack of responsiveness and rigidity, and does not have the high levels of expertise that the FASB has.

The principle that our economy relies on is free enterprise, and the accounting standard setting system should follow this principle. The economy is greatly affected by accounting standards. Letting politics govern the standards that influence the economy would be undermining the free enterprise system.

The accounting standard setting process should remain in the private sector. The rules affect the private sector the most; and it is the private sector that is better able to judge its possible affects. The best way to devise a new standard, or improve an old one, is to let those who best know how it will effect the accounting process evaluate it.

Endnotes

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3. Norris, Floyd. "Politicians Threaten Accounting Integrity." New York Times sec. 3, p.1.
4. Beresford, Dennis R. "What's Right With the FASB." Journal of Accountancy, Jan. 1990, p.82.
5. <http://raw.rutgers.edu/raw/fasb/news//nov30.htm>
6. Van Riper, Robert. Setting Standards for Financial Reporting. Quorum Books. Westport, CT, p.6.
7. Nikolai and Bazley. Intermediate Accounting. 7th ed. Ohio: SouthWestern College Publishing, 1997, p.3.