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**Principles (FASB) versus Rule Based Accounting (IFRS)**

**2.**

Generally, standards set by the Financial Accounting Standards Board (FASB) are principles based. Such a standard has come under criticism due to large accounting scandals such as Enron, WorldCom, and most recently, Lehman Brothers. Rule based accounting, as in International Financial Reporting Standards (IFRS), provides detailed rules that accountants must follow. In theory, a rules based system should increase accuracy and reduce interpretive accounting by management. Such a system could provide more reliable accounting by increasing neutrality, validity, and representational faithfulness. A rules based system, however, may cause unnecessary complexities in financial statement preparation. Also, a “one size fits all” system may not be appropriate for every industry. From a practical standpoint I believe that the SEC should move to convergence, rather than full adoption of IFRS. Changes to Generally Accepted Accounting Principles (GAAP) can be made slowly as needed. Full adoption of a new accounting standard would reduce the comparability of historical and current financial information. Changes to the present accounting system must be made slowly, so the industry can adapt educational and reporting standards.

In order for financial statements to be comparable, there must be only one system of GAAP. I agree with the Former Chairman Arthur Levitt that, “The menu system, I believe, leads to earnings management, and that should be avoided."[[1]](#footnote-1) Whatever accounting system that is decided upon, all industries should adopt the same principles. Allowing American companies to select GAAP versus IFRS not only leads to earnings management, but comparability issues. One uniform system allows end users to compare financial performance to the past and to other similar companies. An adoption of an entirely new system would also not likely be applied uniformly industry wide. There are not enough qualified accountants to make such an overnight switch.

Currently the Certified Public Accountant Examination (CPA Exam) does not cover IFRS for 2010. Also, universities teach very relatively little information regarding IFRS. It is not practical to switch accounting standards too quickly, as the industry is already adopting continually changing standards. Self regulatory industry groups and the legal system has decades of dealing with the current system. Prior case law, text books, and interpretations have been created around the older system. In order to adopt new standards, I agree with the National Association of State Boards of Accountancy to move towards convergence.

Pronouncements have been the natural way in which US GAAP has adapted over time to fit the needs of industry and users. There is no reason that GAAP cannot slowly comply to standards which better suit the globalized economy and industry. Slow adoption would reduce the administrative burden on companies, investors, teachers, and industry professionals. The result would be a slow change in the accounting system with quality and uniform application of the rules.

Accounting standards will continue to evolve as needed, as they have been evolving for generations. A “cold turkey” approach to abandoning GAAP would be a disaster. Just as industry did not switch to the metric system overnight, industry will not switch accounting standards overnight. Changes will be made and developed as needed, not forced. Regardless of the merits of any new system, accountants are still constrained to creating comparable financial statements within a certain degree of cost benefit standards. The slow adoption of new rules is the best way to accomplish constructive changes.

1. Ciesielski, Jack. “The SEC’s IFRS Proposal: Be Careful What You Wish For”

   Seeking Alpha. May 7, 2007. Web. 27 April 2010.

   http://seekingalpha.com/article/34737-the-sec-s-ifrs-proposal-be-careful-what-you-wish-for [↑](#footnote-ref-1)