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Comment Letter

December 10, 2002

TO: FINANCIAL ACCOUNTING STANDARDS BOARD
FROM: CHRISTOPHER BOLE
SUBJECT: CONSIDERATION OF PRINCIPLES-BASED APPROACH TO U.S.
ACCOUNTING STANDARD SETTING

This memo is in response to your proposal for public comment on a principles-based approach to accounting standard setting. As a senior at Providence College, I am writing this memo not only as part of my final grade, but also on behalf of the millions of investors that have not taken this opportunity to make the FASB aware of pertinent issues in considering the aforementioned principles-based approach.

There are several issues that pose significant questions when considering the application of a principles-based approach to U.S. Accounting standard setting. First, it must be recognized that principles would result in rare exceptions, if any, since the concepts would be so broad. When should income and expenses be recognized? For example, the matching principle exists to keep companies from inflating net income from one reporting period to the next. If accounting principles are instituted in the U.S., how is income measured and when will it be implemented in the absence of finite rules? These permanent principles make it hard for implementation. In addition to the question of implementation is the uncertainty of who enforces these new principles. It seems as if rules may be needed in correlation with principles to ensure sound accounting standards for regulators to enforce. Similarly, the challenges of comparability and consistency loom large for proponents of the principles-based approach. Will Boeing recognize the same amount of income on a multi-year jet production contract under the percentage of completion method for the principles-based approach? How will this figure compare with its competitors? More importantly, the outcome for this potential change applies more weight to the

auditors' opinions as to whether they believe the principles apply in good faith consistent with the intent and spirit of the standards.

In subtlety, many of the questions that are raised by changing to principles are the very same issues that highlight why keeping our current system of rules, bearing a few alterations, is not such a bad idea. With the passing of a principles-based approach, the SEC would have to work twice as hard to ensure the judgments of auditors are legitimate. In other words, rules (like the ones we currently have in place) would limit the SEC second-guessing professional judgements. As mentioned earlier, rules also provide for a benchmark of enforcement. What sense does it make to have broad standards if there are no finite measurements to push against?

Part of the reason why consideration is being given to broader standards is because we all recognize that the current standards are not sufficient to prevent corporate malfeasance. To cure this problem, conclusions must be reached on a few outstanding issues. The debate of reliability and relevance, otherwise known as accounting versus economic substance, is a significant dilemma that renders consideration. Should market value (fair value) rather than historical cost be used as the basis for financial statement disclosures? Market value not only provides more relevant financial information to users who are trying to make investment decisions, but also prevents nonsensical transactions that companies make to alter the cosmetics of its balance sheet. A piece of appreciated real estate may be sold because the current rules dictate it be reported at the lower of cost or market value. If real estate were to be reported at market value, then corporate decisions may be made based on economics rather than because of accounting rules, and benefit investors in the long run.

Similarly, the accounting rules for stock option expensing should be reconsidered. The current loose standards for disclosure of stock-based compensation plans ignore consistency and comparability across industries. As an investor, seeing Company A expense stock options and Company B not expense does not provide the stakeholders with fair grounds to compare results. Thus, the controversy over treatment of stock options deserves more attention, and perhaps a resolution.

In sum, companies will always find ways to circumvent new standards. History has shown that the economy has moved in cycles from regulation to deregulation and back to regulation. Given these set of facts, the question becomes: What set of accounting standards is going to provide the best financial reporting in the long run? It is hard to imagine that a few bad

apples can spoil the barrel, and that we can suddenly ignore the sound job our current system has provided us in its lifespan. Thank you for your time. I would appreciate any feedback on your roundtable discussion on December 16, 2002.

CHRISTOPHER BOLE