December 11, 2002

TO: FINANCIAL ACCOUNTING STANDARDS BOARD
FROM: CHRIS NABHAN
SUBJECT: PRINCIPLES-BASED APPROACH

My name is Chris Nabhan and I am an accounting major at Providence College. Recently our class has been discussing the proposed shift by the FASB to implement a more principles-based approach to accounting standards. As part of our final exam, our class has been asked to inform you of our feelings regarding the proposed change.

In the wake of a series of accounting scandals in recent years, a great deal of pressure has been placed on the FASB to implement a system that will reduce corruption in the accounting practice. In order to reduce fraud within the accounting industry, there must be an adoption of a principles-based approach. The new approach will disclose information in a timelier manner, therefore providing information to decision makers while it still makes a difference. The new principles will apply more broadly across the accounting standards, therefore providing fewer exceptions to the principles.

The detailed guidance of principles-based accounting will prevent companies from seeking refuge behind the loopholes of the law. Many of the malpractices uncovered in recent months fell within the established rules. It will provide less interpretive and implemental guidance, which will create an industry in which auditors will be forced to exercise value judgments that will benefit the public. The new change will improve the quality and transparency of U.S. financial accounting, by creating a system that will be easier to understand. The principles-based approach will more clearly disclose the economic substance events, thereby making corruption and fraud more evident. In recent years, companies such as 3Com and Yahoo have adopted Pro Forma earnings. The result has been financial statements littered with inflated revenues. These numbers deceived investors and created a series of values that would have been prevented through the new, principles-based approach.

One of the changes created by the proposal will create a shift from fair-value accounting to market value accounting. Fair-value accounting allows for greater manipulation as displayed in the Enron scandal. Enron inflated its assets by recording a
fair-market value that was higher then the book value. The problem creates a trade-off between reliability and relevance. While the companies disclose values that confirm prior expectation, they are not necessarily display verifiability or representational faithfulness. The shift will create a more honest valuation in which companies have less of an opportunity to deceive investors.

I hope you will take time to recognize the opinions sent forth by my fellow classmates and myself, and hopefully respond to our concerns.