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COMPANY RESISTANCE TO COMPLEX FASB STATEMENTS—THE CASE OF SFAS 33*

*Kenneth Rosenzweig, Ph.D., CPA***

Over the past fifteen years, the Financial Accounting Standards Board (FASB) has issued numerous pronouncements designed to narrow the differences in accounting practice and thereby increase the usefulness of financial statements by making them more comparable among different enterprises. Though questions have often been raised over the years about the complex and prescriptive nature of these pronouncements, Statement of Financial Accounting Standards No. 33, "Financial Reporting and Changing Prices," (SFAS 33) has perhaps been the most controversial. The above statement required subject companies to generate and publish information that was radically different from that produced in accordance with conventional financial reporting practices. As a consequence, such companies could be expected to have devoted considerable resources to the implementation of the requirements and to rely on outside resources such as consulting firms for expertise which did not exist internally.

This study reports the results of a questionnaire survey of companies subject to SFAS 33. The results of the survey show that, contrary to expectations, these companies have generally devoted relatively few employees and manhours to the development of the required information and frequently have used less refined and cheaper methods for producing it. The study also provides some data indicating that, for the most part, companies had little commitment to the implementation of the statement, which may account for the lack of resources assigned to constructing the required information. The findings of the study suggest the more general conclusion that, contrary to the FASB's intention, the complexity of FASB pronouncements may have often decreased the usefulness of financial statements by straining the resources of companies' accounting systems and reducing the commitment of accountants to producing information they considered to be of questionable value. This lack of commitment, along with the greatly reduced inflation rates in the 1980's, may have been significant factors in the FASB's decision to make SFAS 33 disclosures entirely voluntary (Statement of Financial Accounting Standards No. 89, 1986).

BACKGROUND

The attempts by the accounting profession to deal with the distorting effects of price changes on reported financial information have been characterized in recent years by a number of developments. The limited requirements of ASR 190 (Securities and Exchange Commission, 1976) were significantly modified and expanded by SFAS 33. Information required by that statement was seen as a possible solution to the problem of capital impairment resulting from the use of inflated historical-cost-based income numbers for purposes such as dividend and pricing decisions by management. However, an article based on the same questionnaire survey as this article conducted in 1983, four years after the implementation of the statement, found the use of SFAS 33 information by management to be minimal.¹

The purpose of the study reported in this article is to examine the minimal preparation by companies for compliance with the requirements of SFAS 33 in terms of resources employed, methods used, and outside assistance acquired. This minimal preparation may have led to the production of less precise information which would generally not have been utilized by financial statement users.

Information was collected for this study by means of a questionnaire sent to companies subject to the reporting requirements of SFAS 33. The questionnaires were mailed to the controllers of all companies on the FASB Statement 33 Data Bank² in late 1983. Usable responses were received from 544 companies, which represents a response rate of 37%.

RESEARCH FINDINGS

The following section analyzes the resources employed and the related degree of effort expended by companies in developing the information required by SFAS 33.

Resources Devoted to Developing SFAS 33 Information

The companies were asked how many company professional employees had as their primary task the develop-

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ment of the first year's SFAS 33 information and how many manhours were devoted to that task. Tables 1 and 2 summarize the numbers of companies with various numbers of employees and numbers of manhours devoted to developing the first year's information.

Over 70% of the companies devoted two or fewer employees and 600 man hours or fewer to developing the first year's SFAS 33 information. Given that the companies subject to the statement are among the largest in the United States (averaging approximately 100,000 employees), this seems to be a very small use of resources.

Further analysis revealed that larger companies, in terms of number of company employees, generally assigned more employees to develop SFAS 33 information than smaller companies, either because they had more resources available or because of the greater complexity of their task. Also, companies that had been subject to ASR 190 were more likely to assign higher numbers of manhours to develop SFAS 33 information, perhaps because their prior experience with ASR 190 price adjustments made them appreciate the difficulties of that adjustment process.

The number of employees who developed the information and the manhours devoted to the task were found to differ considerably with the companies' industrial classification.

The above information was calculated for companies in major industrial categories of the Standard Industrial Classification.³ Manufacturing companies assigned materially greater number of employees (10) and manhours (1,128) to developing the first year's SFAS 33 information

Table 1

Number of Employees Whose Primary Task was Developing the First Year's SFAS 33 Information

Number of Employees	Number of Companies	Percent of Companies
0	65	13
1	164	32
2	132	26
3	51	10
4	26	5
5	24	5
6 and above	44	9
	<u>506</u>	<u>100</u>

Table 2

Number of Manhours Devoted to Developing the First Year's SFAS 33 Information

Manhours	Number of Companies	Percent of Companies
0 - 200	193	40
201 - 400	85	18
401 - 600	69	15
601 - 800	28	6
801 - 1000	32	7
Above 1000	69	14
	<u>476</u>	<u>100</u>

Table 3

Predominant Method to Develop Current Cost for Property, Plant, and Equipment

	Number of Companies	Percent of Companies
No direct valuation:	434	84
Price indexes		
Direct valuation methods:	43	8
Direct pricing		
Unit pricing	24	5
Function pricing	15	3
	<u>516</u>	<u>100</u>

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Table 4
Valuation Methods for Property, Plant, and Equipment
Chosen by Companies for Major Industrial Categories

	No Direct Valuation	Direct	Valuation	Methods	
	Price Indexes	Direct Pricing	Unit Pricing	Functional Pricing	Total
Retail Trade:					
Number of companies	16 (49%)	2 (6%)	13 (39%)	2 (6%)	33 (100%)
Transportation, communication, electric, gas, and sanitary services:					
Number of companies	114 (82%)	16 (12%)	4 (3%)	4 (3%)	138 (100%)
Finance, insurance, and real estate:					
Number of companies	59 (89%)	2 (3%)	3 (5%)	2 (3%)	66 (100%)
Manufacturing:					
Number of companies	139 (91%)	7 (4%)	1 (1%)	6 (4%)	153 (100%)

than companies in other industrial categories. In contrast, companies in transportation, communication, electric, gas, and sanitary services assigned three employees and utilized 714 manhours; retail companies assigned two employees and used 720 manhours; and companies in finance, insurance, and real estate assigned two employees and utilized 244 manhours. Further analysis revealed that differences in the average size of companies in the different industries does not account for the differences among industries in resources assigned to developing SFAS 33 information.

In-House Effort

SFAS 33 represented the most revolutionary change in U. S. financial reporting practices in recent history. Most of the techniques required to develop the information had not formerly been used by companies for financial reporting. Since the expertise needed was probably not available in house, it seems logical that many companies would have turned to outside experts for assistance. However, the survey results indicated that 93% of the total effort was performed in house, 5% by CPA firms, 1% by non-CPA firm consultants, and 1% by others.

In spite of the presumed absence of expertise for developing the information, companies relied heavily on internal resources to satisfy the requirements of SFAS 33. Perhaps outside consultants were equally baffled by the new information and could provide only limited assistance. Also, companies may have been hesitant to pay for assistance in developing information they did not consider useful.⁴

Measurement Methods

SFAS 33 allowed companies considerable discretion in the choice of methods for developing the information. The choices extend from those which would produce the most

useful information but would require the application of considerable resources to those that would require less resources but would produce less useful information. As an index of the overall complexity of adjustment methods used, the companies were asked which of four methods was the predominant one used to develop current costs for property, plant, and equipment. The methods discussed in SFAS 33 (pp. 19–21), are price indexes, direct pricing, unit pricing, and functional pricing. It was assumed that the use of price indexes required considerably less effort than the use of the other three methods—since the latter require a direct valuation of individual assets—while price indexes can be applied to assets of different age groups without a direct valuation.

Table 3 shows that the vast majority of companies used price indexes which are assumed to be the least sophisticated of the valuation methods available. It can, therefore, be inferred that many companies sacrificed usefulness of the information in order to minimize the costs of its development.

The choice of valuation method differed considerably by industrial classification. Table 4 shows the number of companies in major industrial categories that chose the various methods.

Table 4 reveals that companies in the retail industry had a much lower tendency to use price indexes for valuation than companies in other industries. This is surprising because the retail industry is likely to have had more experience with price indexes prior to SFAS 33 than companies in other industries since the commonly used retail inventory method employs them. Another unanticipated finding is that companies in the manufacturing industry tended to make heavy use of price indexes. Since manufacturing companies were shown to devote more resources in terms of employees and manhours to the development of SFAS 33 information, it might have been expected that they would also tend to use the more sophisticated direct valuation methods.

Formal Use Policy

There has been much debate in the accounting community about the advisability of adjustments for changing prices. Companies have differed in the extent to which they believed such information was needed for financial reporting. Companies that believed the information was needed may have felt a commitment to the full implementation of the requirements that was not felt by other companies. It seems logical that many companies that felt such a commitment would encourage the use of the information for internal purposes by establishing a policy that the information be used. Therefore, as a measure of the extent of commitment of their companies to the adjustment process, the respondents were asked whether the top management of their companies had a formal policy that the information be used internally. Only ten companies (2%) indicated that they had a formal use policy. If the existence of such a policy is any indication of the extent of company commitment to the implementation of SFAS 33, the results suggest most companies produced the information reluctantly and only because it was required.

CONCLUSION

Why did companies generally devote minimal effort and resources to implementing SFAS 33? One can only guess at the answer. However, the study provides some evidence that companies, in general, had little commitment to the implementation of the statement and, perhaps, little faith in the validity of the information produced as a result of it.

This lack of commitment to, and faith in, the statement is consistent with other findings⁵ that companies, in general, had very little use for SFAS 33 information for internal purposes. Moreover, the lack of commitment of companies to SFAS 33 may be only one illustration of the more prevalent lack of support in the accounting community for excessively complex accounting standards which generate information considered to be of questionable value. The recent action of the FASB to make SFAS 33 disclosures voluntary may, therefore, have been partially a response to the general dissatisfaction with such standards, although reduced rates of inflation in recent years obviously made the decision more palatable.

Endnotes

¹Rosenzweig, Kenneth, "Companies Are Not Using SFAS 33 Data," *Management Accounting* (April, 1985), pp. 51-57.

²Vasarhelyi, M., A. N. Phillips, and D. C. H. Yang, *FASB Statement 33 Data Bank, User's Manual* (New York: Value Line Investment Survey, 1983).

³*Standard Industrial Classification Manual*, Executive Office of the President, Office of Management and Budget (Washington: U.S. Government Printing Office, 1972).

⁴Rosenzweig, loc. cit.

⁵*Ibid.*