## Contents

<table>
<thead>
<tr>
<th>Week 1: Introduction to Accounting Theory</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Four KEY Questions in Financial Reporting</td>
<td>3</td>
</tr>
<tr>
<td>Theories</td>
<td>3</td>
</tr>
<tr>
<td>How to exercise our Judgement</td>
<td>4</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Week 2: Ethics and Accounting Policy Choice</th>
<th>Error! Bookmark not defined.</th>
</tr>
</thead>
<tbody>
<tr>
<td>What is Ethics?</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>2 perspectives of ethical judgements:</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Fundamental Ethical Principles</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Three Core Skills in Practical Ethics</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>The DECIDE Model</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>The POLICY Model</td>
<td>Error! Bookmark not defined.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Week 3: Measurement</th>
<th>Error! Bookmark not defined.</th>
</tr>
</thead>
<tbody>
<tr>
<td>What is Measurement?</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Objectivity and the Components of Accounting Measurement:</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>4 key components of the measurement process (and some questions to consider):</td>
<td>Error! Bookmark not defined.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Example: Measurement in Accounting</th>
<th>Error! Bookmark not defined.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Historical Cost vs Some Form of Current Value</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>What does it matter how me measure A&amp;L?</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>What do we Measure</td>
<td>Error! Bookmark not defined.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Week 4: Fair Value</th>
<th>Error! Bookmark not defined.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Importance of FV</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>What is Fair Value?</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>The “HIERARCHY” of Estimation Methods</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Categories of Financial Instruments</td>
<td>Error! Bookmark not defined.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Week 5: Revenue</th>
<th>Error! Bookmark not defined.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Week 6: True and Fair View</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Courts and True and Fair</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Truth in Accounting</td>
<td>Error! Bookmark not defined.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Week 7: Economic Incentives</th>
<th>Error! Bookmark not defined.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Entity View</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Nexus of Contracts</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Agency Theory</td>
<td>Error! Bookmark not defined.</td>
</tr>
<tr>
<td>Manager – Shareholder Agency Relationship</td>
<td>Error! Bookmark not defined.</td>
</tr>
</tbody>
</table>
Manager – Debt holder Agency Relationship ................................................................. Error! Bookmark not defined.
Additional Disciplining Measures for Managers .......................................................... Error! Bookmark not defined.
Week 8: Capital Markets Research ................................................................................. Error! Bookmark not defined.
Efficient Market Hypothesis .......................................................................................... Error! Bookmark not defined.
Levels of Market Efficiency .......................................................................................... Error! Bookmark not defined.
Role of Evidence ............................................................................................................ Error! Bookmark not defined.
Empirical Research in Accounting ............................................................................... Error! Bookmark not defined.
Costly Contracting – A Reminder ................................................................................ Error! Bookmark not defined.
Capital Market Research .............................................................................................. Error! Bookmark not defined.
Week 9: Behavioural Accounting Research ................................................................. Error! Bookmark not defined.
Brunswick Lens Model vs. Process Tracing ..................................................................... Error! Bookmark not defined.
Baye’s Theorem ............................................................................................................. Error! Bookmark not defined.
Heuristics & Biases ....................................................................................................... Error! Bookmark not defined.
Social and Environmental Reporting ............................................................................ Error! Bookmark not defined.
Terminology and Definitions ......................................................................................... Error! Bookmark not defined.
A Theoretical Framework for Corporate Social Responsibility .................................... Error! Bookmark not defined.
Emission Trading Schemes .......................................................................................... Error! Bookmark not defined.
Week 11: Regulation of Financial Reporting ............................................................... Error! Bookmark not defined.
   Traditional criticisms of accounting ........................................................................ Error! Bookmark not defined.
   Characteristics of Modern Capital Markets .............................................................. Error! Bookmark not defined.
   Market forces as a means of corporate controlling ................................................ Error! Bookmark not defined.
   Analysis of Arguments for Regulation ..................................................................... Error! Bookmark not defined.
   Impact of Informational Asymmetries ...................................................................... Error! Bookmark not defined.
2. How to Regulate Accounting .................................................................................... Error! Bookmark not defined.
   Self Regulation? ....................................................................................................... Error! Bookmark not defined.
Week 12: International Convergence of Accounting Standards .................................... Error! Bookmark not defined.
The International Accounting Standards Board (IASB) ................................................. Error! Bookmark not defined.
International Harmonisation ........................................................................................ Error! Bookmark not defined.
De Jure Harmonisation ................................................................................................ Error! Bookmark not defined.
De Facto Harmonisation ............................................................................................... Error! Bookmark not defined.
Political Process .......................................................................................................... Error! Bookmark not defined.
Importance of US GAAP ............................................................................................ Error! Bookmark not defined.
Week 1: Introduction to Accounting Theory

Four KEY Questions in Financial Reporting

1. **Definition**: WHAT was the transaction about
   a. **Definition / Components** – e.g. what are the A&L etc. is the transaction a “sale” or a “financing” transaction (e.g. sell building to financing company and lease it back – in its form this is a sale and lease back, but in its substance this is a financing transaction because they continued to operate in it)?

2. **Recognition**: WHEN did it occur?
   a. **Recognition** – when should the components of the transaction be entered into the accounting records? When should income be recognised?

3. **Measurement**: HOW MUCH?
   a. **Measurement** – e.g. should the transaction be recorded at cost, fair value, replacement cost, present value, NRV etc? – this effects the amount of gain going into each period

4. **Disclosure**: WHAT ELSE do we need to know
   a. **Disclosures** – is extra information required to inform readers about transactions that were ‘recognised’ and those that were not recognised? E.g. related party transactions, risk and uncertainty.

The answers to the questions above are found in an entity’s “Accounting Policies” – which is defined in AASB 108 para 5 as: “the specific principles bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements”. Accounting Policies always in Note 1 & 8 of financial report

**How do we know if our Accounting Policies are “Good”?**

- The exercise of “professional judgement” is necessary in the real world because:
  - Modern transactions are complex and involve constant innovation
  - Accounting standards don’t cover all types of transactions
  - Accounting standards can be ambiguous (e.g. relevance and reliability)
  - Accounting standards still offer some choices (e.g. depreciation methods, cost flow assumptions in inventory accounting etc)

- What drives our Judgement?
  - The AASB Framework lists qualititative characteristics necessary for accounting information to be “decision useful”
    - Understandable (para 25)
    - Relevance (para 26-30)
      - Materiality
    - Reliability (para 31 – 38)
      - Faithful representation, Substance over form, Neutrality, Prudence, Completeness
    - Comparability (para 39-42)

- What if our judgement is wrong?
  - Loss of public confidence, Movements in wealth, Damage to reputation, Fines, Jail

**Theories**

Theory is typically a set of propositions from which we reach our conclusions and decisions. When we exercise our professional judgement, we are applying a theory.

There are 2 types of theories:

1. **‘positive’ theories** – describe how people do act, regardless of if its good or not and explain why people act like this
2. **‘normative’ theories** – are prescriptive – they describe how people should act in order to achieve a ‘good’ outcome
These two theories can assist each other. For example, normative theorists say how we should classify a certain lease and then positivists test this to see how accountants actually are testing it. Or positive theory can provide an understanding of the role of accounting which, in turn, can from the basis for developing normative theories to improve the practice of accounting.

**Strengths of Positive theory over Normative theory**
- We need to know how the world works before prescribing normative theories.
- Normative theories have been criticised for making presumptions which are not based on indentified, empirical observations or methods.
- A positive example of an objective function is the specification of how the measurement of assets at their current cost affects the distribution of wealth between shareholders, lenders and managers. In turn, the positive theory could be used in developing a normative theory of why accountings should or should not measure assets at current cost.

How positive accounting theory has remedied the defects of normative accounting theory...
1. It was perceived that theory should be able to generate hypotheses capable of falsification through empirical testing.
2. It was deemed desirable that theory aim, firstly, to explain and predict accounting practice rather than supply prescriptions. This overcame the need to supply an objective.
3. It was necessary to assess existing accounting principles, which normative accounting theory did not attempt to do in any systematic empirical manner (no objective is superior).
4. It is one of the imperatives of positive accounting theory that there be some attempt to model the connection between accounting, firms and markets and to analyse problems within an economic framework.

**How to exercise our Judgement**
- We won’t be found to have done wrong unless we exercise our judgement negligently or fraudulently
- accounting policy choices must;
  - be made systematically
  - reflect appropriate rules and concepts
  - reflect available facts
  - reflect professional values and ethics. E.g.
    - objectivity, independence, competence, integrity etc
  - be JUSTIFIABLE

- **A Basic Accounting Policy Choice Decision Model**
1. Identify the relevant facts
   - a. Including key stakeholders (distinguish known facts from assumptions, identify the factors that are ‘unknown’)
2. Define the accounting policy issues – how to classify and measure
3. Identify relevant accounting standards, rules, and principles
4. Identify alternative accounting policies (e.g. cost or revaluation model)
5. Evaluate alternative accounting policies (benefits and costs of those models – short and long term consequences)
6. Make a choice (MUST make a decision) that maximises positive – or minimises negative – consequences.