

# **PERCEPTIONS OF ACCOUNTING STUDENTS REGARDING FINANCIAL REPORTING AND THE USEFULNESS OF A FINANCIAL REPORTING PROJECT**

**Marianne L. James, California State University, Los Angeles**

## **ABSTRACT**

*Recent financial reporting scandals have enhanced the attention focused on the importance of high quality financial reporting. Accounting professionals must be very knowledgeable about financial reporting requirements and be able to prevent and detect misstatements and omissions. Fundamental financial reporting knowledge and skills should be developed by accounting majors while they are completing financial accounting classes. Yet, deficiencies in accounting students' fundamental financial reporting knowledge have been observed by accounting faculty.*

*This study investigated intermediate and advanced accounting students' perceptions regarding financial reporting, and the effect of completing a financial reporting project requiring analysis of errors and omission on those perceptions. One hundred sixty-four students enrolled in intermediate and advanced accounting classes completed a financial reporting project and pre and post-project questionnaires.*

*Students at all levels reported significantly increased confidence regarding financial reporting, after completing a financial reporting project. A project requiring analysis of financial statements containing errors and omissions may be useful to enhance students' confidence in their financial reporting abilities, and may also enhance their analytical and problem solving skills as recommended by the AICPA's Core Competency Framework.*

## **INTRODUCTION**

Recent financial reporting scandals involving large public companies, such as WorldCom and Enron have focused renewed attention on the need for high quality and reliable financial statements. Chief executives and financial officers of large public companies are now required to certify the accuracy of annual and quarterly financial statements filed with the Securities and Exchange Commission (SEC, 2002). This requirement represents just one of the major provisions of the newly legislated Sarbanes-Oxley Act of 2002 passed by the U.S. House and Senate on July 25 and signed into law by President Bush on July 30, 2002, affecting the accounting and audit profession.

Accounting professionals must be very knowledgeable and skilled regarding financial reporting. Financial statement preparers must be able to prepare financial statements that are free of material misstatements or omissions, and financial statement auditors must be able to detect misstatements and identify omissions of relevant information. Even financial statement users, such

as investors and analysts are likely to benefit from knowledge of fundamental financial reporting concepts.

To prepare for a challenging profession, students majoring in accounting should acquire fundamental financial reporting skills and knowledge while completing their financial accounting classes. However, accounting faculty at a Western public university business school have observed that undergraduate accounting students frequently experience difficulty in preparing basic financial statements and disclosures. In addition, students frequently lack confidence in their financial reporting knowledge and may avoid completing financial reporting assignments. To help accounting students acquire financial reporting knowledge and skills, and gain confidence in their abilities, a financial reporting project that contained errors and omissions was developed and utilized in intermediate and advanced accounting classes. Prior to working on the project and two weeks after completing the project, students were asked to rate how comfortable they felt reviewing and analyzing financial statements in terms of four aspects of financial reporting.

Students' self-reported mean ratings on questions addressing four facets of financial reporting ranged from 2.09 to 2.96 prior to working on the project, with the lowest mean rating associated with note disclosures. No significant difference was found in students' mean ratings between higher and lower level financial accounting classes. Students' mean ratings were significantly higher after completing the financial reporting project, than they were prior to working on the project ( $p$ -values $<0.05$ ). Mean ratings ranged from 2.97 to 3.53, with the lowest rating again being associated with note disclosures. This suggests that the project tended to improve students' confidence in their financial reporting knowledge and skills. Since financial reporting knowledge and skills are expected to remain of paramount importance, students are likely to benefit from a project that requires critical analysis of actual financial statements.

## **REVIEW OF THE LITERATURE**

For more than a decade, public accounting firms and other employers of entry-level accounting professionals have criticized accounting graduates' non-technical skills, such as communication, analytical/critical thinking, leadership and professional interpersonal skills. However, technical accounting skills continue to be of paramount importance. In a recent landmark study by Albrecht and Sack (2000), practitioners and educators ranked the type of services that they expected accounting graduates to perform five years from now. Practitioners ranked financial reporting third after financial analysis and financial planning, while educators ranked auditing first, followed by e-commerce and strategic consulting. Novin and Pearson (1989) surveyed CPAs in public practice and found that 94 percent of the respondents felt that university instruction in financial accounting and reporting concepts and 81 percent that instruction in financial reporting practices should not be reduced. Accounting students also are aware of the need for financial reporting knowledge. A survey of accounting students (Usoff & Feldman, 1998) found that students consistently rated accounting knowledge, of which financial reporting is an integral part, as the most important skill necessary for career success.

Recent events involving large public companies have intensified concern regarding the quality of financial reporting. Consistent with the Sarbanes-Oxley Act of 2002, CEOs and CFOs now must certify their company's annual and quarterly reports filed with the SEC (H.R 3763, 2002).

On June 27, 2002 the SEC published a list of 947 companies with revenues in excess of \$1.2 billion, whose CEOs and CFOs must certify their companies' financial statements; to date, the majority of firms have complied with the August 14, 2002 deadline (SEC, 2002).

Fundamental financial reporting skills must be developed by accounting majors while they complete their financial accounting classes. Accounting faculty at a Western public university have observed a basic lack of familiarity with, and understanding and knowledge of financial reporting concepts and requirements among undergraduate accounting students at all levels. In addition, accounting majors also appear to feel little confidence in their financial reporting knowledge and skills and may avoid completing financial reporting assignments. Knowledge and understanding of financial reporting is important in many business settings. Individuals who possess good knowledge of financial reporting, are likely to benefit from such knowledge in a number of different capacities: as financial statement preparers, auditors, and users.

To address this problem and to help accounting majors prepare for a challenging profession, accounting students should be exposed to financial reporting in a manner that supports understanding and learning of reporting requirements and concepts, and also helps them feel comfortable and confident about their abilities.

In its 2001 exposure draft to change the structure of the Uniform CPA Examination, the American Institute of Certified Public Accountants (AICPA) included skills that are "necessary for the protection of the public interest include the ability to communicate, the ability to perform research, the ability to analyze information, and the ability to organize information, as well as other higher-order skills" (p.14). Strategic and critical thinking, which includes "the ability to link data, knowledge, and insight together from various disciplines to provide information for decision making," are included in the AICPA's Core Competency Framework for Entry in the Accounting Profession as one of Broad Business Perspective Competencies (AICPA, 2002). Included under Personal Competencies are "effective problem-solving and decision-making skills, good insight and judgement" (AICPA, 2002).

The AICPA has also developed "Sample Teaching Strategies and Classroom Techniques That Address The Core Competencies" including problem-based learning cases which are described as "Students use knowledge, concepts, and skills relevant to a course to solve realistic business problems" (AICPA, 2002). The financial reporting project, which was utilized in several intermediate and advanced accounting classes incorporates use of analytical/strategic, problem-solving and communication skills.

## **RESEARCH PURPOSE AND METHODOLOGY**

The purpose of this study was to investigate (1) accounting students' perceptions regarding their financial reporting skills and knowledge, and (2) changes in those perceptions after completion of a financial reporting class project.

The project was developed by the researcher/instructor and consisted of a set of comparative financial statements with accompanying notes of typical and realistic content, length and format for a hypothetical consolidated company. The financial statements and notes contained a number of errors and omissions. Prior to utilizing the project, a colleague and an accounting professional with many years of audit and financial reporting experience reviewed the project's validity. Based on

their feedback, a few modifications were incorporated into the project. At the beginning of the courses, students enrolled in Intermediate Accounting I, II, III, and Advanced Accounting were asked to report their comfort levels regarding financial statements and disclosures. Students were assured that their responses were anonymous and would have no bearing on their course grade. Four questions were posited:

1. How comfortable do you feel reviewing/analyzing financial statements in terms of overall financial accounting?
2. How comfortable do you feel reviewing/analyzing financial statements in terms of overall financial reporting requirements?
3. How comfortable do you feel reviewing/analyzing financial statements in terms of specific financial statement elements?
4. How comfortable do you feel reviewing/analyzing financial statements in terms of adequacy of note disclosures for specific accounting issues?

A five-point Likert scale with 5 representing very comfortable, and 1 representing not very comfortable was utilized. The students were instructed to work on the project for eight weeks and identify the errors and omissions that related to the subject material covered in their class, and to suggest the appropriate accounting treatments and complete or correct the disclosures. Two weeks after completing the project and submitting their written reports, the students were again asked to assess their level of comfort with financial reporting issues.

## RESULTS

Students' mean comfort ratings associated with analyzing financial statements in terms of overall financial accounting ranged from 2.50 to 2.77, prior to working on the financial reporting project, and from 3.34 to 3.53, after working on the project. Students' mean comfort ratings associated with analyzing financial statements in terms of overall financial reporting requirements ranged from 2.42 to 2.65, prior to working on the financial reporting project, and from 3.17 to 3.50, after working on the project.

Students' mean ratings associated with analyzing financial statements in terms of specific financial statement elements ranged from 2.26 to 2.96 prior to working on the disclosure project, and from 3.33 to 3.45, after working on the project. Students' mean comfort ratings associated with analyzing financial statements in terms of adequacy of note disclosures for specific accounting issues ranged from 2.09 to 2.47 prior to working on the disclosure project, and from 2.97 to 3.34, after working on the project.

T-tests of differences in mean ratings showed that in all classes and for all four financial reporting questions, students consistently reported significantly increased comfort-levels subsequent to completing the financial reporting project, than before working on the project ( $p$ -values  $< 0.05$ ). This suggests that the project improved students' confidence in their financial reporting knowledge and skills.

Students who had already completed several intermediate accounting classes did not tend to report higher pre-project comfort levels, than those who had not yet completed Intermediate

Accounting. Thus, it appears that exposure to different financial reporting issues, and advancement in the accounting degree program in itself had little positive effect on students' confidence in their ability to analyze and review financial statements.

## CONCLUSIONS

Prior to completing the financial reporting project, students on average felt less than comfortable analyzing and reviewing financial statements. In addition, mean comfort levels were not significantly higher at more advanced levels, than at less advanced levels of accounting.

After completing the financial reporting, students at all levels consistently reported higher mean comfort levels, suggesting higher confidence in their abilities. Since financial reporting knowledge and skills are expected to remain very important, findings from this study suggest that students are likely to benefit from a project that requires analysis of financial statements that contain some errors and omissions. Higher emphasis on financial reporting aspects, including note disclosures appear to be warranted to prepare accounting students for a challenging profession.

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