Douglas Carmichael is a former chief auditor of the Public Company Accounting Oversight Board and a member of its standing advisory group, so when he speaks, accountants listen. Among the government agencies he’s consulted with on accounting matters are the Securities and Exchange Commission, the U.S. Department of Justice and the Federal Trade Commission. He’s also the Claire and Eli Mason professor of accountancy at Baruch College’s Zicklin School of Business.

Q: In the last bear market, accountants were front and center in scandals like Enron and WorldCom, but nothing like that has happened during the present downturn. How do you explain that?

A: Well, the Sarbanes-Oxley Act did succeed in making auditors more diligent. And I think PCAOB inspections [of accountants’ work] have resulted in important improvements, too. It’s logical to think if accountants know their work will be checked closely by an outside party, they’ll do a better job. It’s interesting that a decade ago, accountants were criticized for not letting investors know there were problems at companies; now they get blamed for forcing huge companies to take huge writedowns. In other words, accountants were blamed before for not being tough enough; now, they’re blamed for being too tough.

Q: Were you disappointed by the Financial Accounting Standards Board’s decision to suspend fair-value accounting for financial institutions when the markets got difficult?

A: I was, but I understand the pressure the FASB was under. Congress was really pushing for the
suspension; the risk was that the FASB would become irrelevant as a standard-setting organization if it
didn’t comply. There’s precedent for that sort of thing: Years ago, oil and gas companies got angry with how
the FASB pushed them to make their accounting more transparent, so the companies lobbied Congress,
which pressured the SEC not to accept the FASB’s accounting standards for oil and gas companies. That
was probably on the minds of people at the FASB when they made their decision concerning banks.

**Q:** The top position at FASB is vacant. What are the most important tasks for the next chairman?

**A:** One of the most difficult tasks is convergence with the International Accounting Standards Board.
Everyone says, “We want convergence at a high-quality standard,” but it’s difficult to avoid concessions that
reduce the quality of accounting for the sake of convergence. There are questions whether IASB is under
too much control by the European Commission. My belief is the new FASB chairman should resist pressure
for convergence too quickly and only make steps that result in high-quality accounting.

Another issue is the need to reexamine the move to fair-value accounting. If you move too quickly and
broadly into valuing assets at their fair market value, you risk sacrificing the reliability you get valuing them at
historic cost. The move to fair-value accounting is particularly important concerning revenue recognition,
which is where the FASB is doing work now. It is looking at ways of permitting companies to recognize
revenue before a product or service is delivered, so long as a fair-value estimate of the revenue is used.

Anything that makes tradeoffs between relevance and reliability concerning revenue recognition worries me.
That’s because in the past, we’ve seen fraudulent reporting overwhelmingly due to misapplication of
principles on revenue recognition.

**Q:** Do you think the accounting profession is generally better than it was a decade ago?

**A:** One of the most encouraging things I’ve seen involves the accounting fraud at Royal Ahold [a Dutch
supermarket conglomerate]. Their auditors at Deloitte got questionable answers from the company, so the
people at Deloitte went to their higher-ups, and they detected the fraud. This is how it’s supposed to work.
Accounting can’t unveil the full dimensions of corporate fraud, but it can detect it by using professional
skepticism.
Q&A: Here’s what’s ahead in changing industry

Accounting guru discusses standards, sees improvement

By Aaron Elstein

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