Exploring the Benefits of Principles Vs Rule-Based Accounting

An Interview with Chairmen Robert Herz (FASB) and Sir David Tweedie (IASB)
by Solomon N. Darwin

As we move from rules to principles, we need to ask the question: will IFRS provide enough safeguards to protect the investors and citizens of the world? We all know that our US GAAP started out as principles, as denoted by the “P” in GAAP. Over time it evolved into a rule-based accounting system, and for good reasons. Should we quickly abandon the years of experience and wisdom behind what has been regarded as the gold standard of financial reporting and join the rest of the world as they try to play catch up with us? Below are some of the questions I asked the chairmen of the two Standard Setting agencies about the challenges and concerns about convergence toward a single set of Global Accounting Standards.

Darwin: Are IFRS strong enough to prevent the Enron’s, the WorldCom’s and something like our current global economic crisis?

Herz: Enron and WorldCom involved massive frauds that included violation of accounting standards. This can and does happen regardless of the particular accounting standards in force. Certainly, we have our fair share of reporting fraud in the United States.

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Sir David Tweedie, Chairman of the International Accounting Standards Board (IASB), champion of an effort to develop a high quality, single set of global financial reporting standards that are used internationally, is the 2008 recipient of the Berkeley Award for Distinguished Contributions to Financial Reporting.

Dean Rich Lyons acknowledged Sir Tweedie’s contributions by presenting the Award before an audience of over 400 accounting professionals, standard setters, enforcers, and academicians at the 19th Annual Conference on Financial Reporting, held at the Santa Clara Marriott on October 24, 2008.

The Berkeley award recognizes individuals in financial reporting that have demonstrated courage, leadership, stewardship, or other meritorious performance in the interest of providing financial information useful to investors in making investment decisions.

As chair of the IASB, Sir Tweedie has taken an active role in developing comprehensive, high quality financial reporting standards that have already been adopted by more than 112 countries. The US Securities and Exchange Commission (SEC) and Financial Accounting Standards Board (FASB) are considering adopting international financial reporting standards (IFRS) in 2011/2012.

Sir David Tweedie was appointed Chairman of the International Accounting Standards Board (IASB) on January 1, 2001. He was educated at the University of Edinburgh where he received his B.Com. in 1966 and Ph.D in 1969, and qualified as a Scottish Chartered Accountant in 1972. Between 1973 and 1978 he was a Lecturer in the Department of Accounting at the University of Edinburgh. Subsequently he served as Technical Director of the Institute of Chartered Accountants of Scotland from 1978 – 1981, National Research Partner, KMG Thomson McLintock (1982 – 1987) and National Technical Partner, KPMG Peat Marwick McLintock (1987 – 1990). In 1990 he was appointed the first Chairman of the UK Accounting Standards Board (1990 – 2000) and the Chairman of the Urgent Issues Task Force.

Sir Tweedie has been awarded honorary degrees by eight British universities, the most recent bestowed by Oxford Brookes University. Oxford Brookes chose Sir Tweedie for his contribution to a field of study and as an exemplary role model for students. The university stated that “His record establishes his standing as the most distinguished member of the profession in the UK”.

He has also received a number of professional awards, including the Institute of Chartered Accountants in England and Wales’ Founding Societies Award for 1997, awarded annually to a member who has made an outstanding contribution in any field of endeavour, and the Chartered Institute of Management Accounting’s CIMA Award 1998 for services to the accounting profession. The CIMA Award is granted to non-members of CIMA who have made an outstanding contribution to the profession. He was also presented an Honorary Fellowship of the Association of Chartered Certified Accountants.
He has been a visiting professor at the University of Lancaster International Centre for Research in Accounting (ICRA), the University of Bristol and the University of Edinburgh.

He was knighted in 1994 for his services to the Accounting Profession by Queen Elizabeth II.

He has been immortalized by Business Week as “The most powerful accountant on the planet”.

When asked about the current crisis and about his future vision pertaining to the globalization for the single set of accounting standards, his response was:

“The crisis sweeping through financial markets has been breathtaking for many reasons. Foremost are the pace at which events have unfolded, and that no country has escaped its wrath. If ever a demonstration were needed of the free flow of international capital, this is it. We should not be surprised. Investors have long sought investment opportunities across the world. My pension fund has investments in more countries than I have visited, and I have travelled widely. It is high time that regulatory and supervisory frameworks caught up. A global crisis requires a global solution. Regional solutions just don’t cut it anymore.

From our inception in 2001, our goal has been a simple one. To develop, in the public interest, a single set of high quality, understandable and enforceable international financial reporting standards (IFRSs) for use throughout the world’s capital markets. Progress has been rapid. Over 100 countries now require or permit the use of IFRSs and this figure is expected to grow to 150 within the next couple of years. Australia, Hong Kong, South Africa and all member states of the European Union require IFRSs, and Chinese standards are substantially based on IFRSs. Canada, India, Japan and Korea amongst others have announced their intention to adopt or converge with IFRSs in 2011, and of course the US SEC has also proposed that a decision on US adoption of IFRSs should be taken in 2011.

There is still much to do. IFRSs are by no means perfect, and we along with the FASB are learning the lessons from the credit crisis. Many years of work to converge US GAAP and IFRSs has resulted in close alignment of the two sets of standards, but similar isn’t sufficient. The two boards have moved quickly to address short term inconsistencies in areas such as the accounting for financial instruments and will step up efforts to create a single set of ‘improved’ IFRSs that build upon the solid foundations of our respective standards.

The speed at which international standards have been taken up provides a clear reminder that closely coupled global financial markets require a common language to articulate business performance. IFRSs are that language.”

Following are the members of the distinguished committee that selected the winner of the 2008 Award:

Dennis Beresford, Professor, Former Chair
Financial Accounting Standards Board

Jack Ciesielski, Owner

Arthur Fliegelman, Vice President
Moody’s Investors Service

Cheryl Graziano
Vice President, Research and Operations
Financial Executives Research Foundation, Inc.

Rich Lyons, Dean
Haas School of Business, UC Berkeley

Rebecca McEnally
CFA Institute

George Staubus, Professor Emeritus
Haas School of Business, UC Berkeley

Michael Sutton, Former Chief Accountant
US Securities and Exchange Commission
At a time when the integrity of financial reporting is more important than ever, the 19th annual Conference on Financial Reporting, held on October 24, 2008 at the Santa Clara Marriott, gathered key global players -- standard setters, enforcement officials, financial executives, practitioners, and academicians -- to address the critical role and future of financial reporting. Topics included the SEC proposal for US companies to adopt international reporting standards; the impact of key regulatory proposals; and ways to improve financial reporting; and promote accounting practices that are useful to investors.

A Congressional proposal to suspend “mark-to-market” accounting to help the nation’s banks and lenders was a key topic discussed by FASB chairman Robert Herz.

When the market is normally active, financial instruments such as mortgage loans and derivatives are “marked” to their fair value. However, given the critical downturn in the recent market, the rule can misrepresent the true value of investments, greatly affecting the balance sheets of banks with major holdings. Opponents of a rule change fear the removal of “mark-to-market” accounting will allow banks to overstate the value of their assets to investors.

As the US financial crisis expands to a global crisis, the CFRM conference discussed the United States’ opportunities and challenges in adopting global financial reporting standards, current challenges in international business, and lessons learned from the subprime debacle.
“The annual conference on financial reporting is always a valuable and enjoyable event. It is an opportunity to be briefed first hand about current developments in the profession by standard makers and regulators. The conference does an excellent job of presenting the perspectives of regulators, preparers, users and auditors. The panels bring home the reality of each current topic with more immediacy than we get by simply keeping up on our technical reading. An example was the discussion between Bob Herz, Sir David Tweedie and Conrad Hewitt about the proposed timetable and challenges of moving to IFRS. It is also a great forum to get caught up with firm alumni, Cal alumni, clients and other professionals in the business.”

John J. McCauley
Partner, PricewaterhouseCoopers LLP

“The quality of any seminar is dictated by the quality of the speakers. I would say that perhaps this is the best line up of speakers in the Bay Area in 2008. It speaks volumes about the organizers and the organization that conducted this seminar. Well Done!!!”

Prabhakar “PK” Kalavacherla
Partner, KPMG LLP
Board Member, IASB (effective January 2009)

“The conference provided an unparalleled West Coast access to the minds of the key regulators and decision makers in the accounting profession. At a time when we are all struggling to digest the legion of new pronouncements that hit our screens, this served as an invaluable event, placing the most complex of concepts in their context and giving us all a glimpse of the issues that will affect and change future reporting standards.”

Andrew Cotton
Americas Director of Software, Ernst & Young LLP
Executive Accounting Program: March 19-20, 2009
International Accounting IFRS Phase 1 Assessment Workshop

Program Designed for:
Chief Financial Officers
Chief Accounting Officers
Financial & General Controllers
Heads of Financial Reporting
IFRS/IAS Project Leaders
Accountants/Corporate Accounting Consultants

Program Learning Objectives
This course uses real-world case studies on the first time Adoption of IFRS, with the aid of illustrative or model financial statements, to equip financial executives to understand the more complex issues facing first-time adopters. The learning objectives include:

• Rules relating to first-time adoption of IFRS.
• Available choices when preparing IFRS financial statements.
• Common list of pitfalls and the do’s and don’ts in detail with real examples.
• Current IFRS requirements.
• Impact of IFRS on financial statement preparation, disclosures and financial performance reports.
• Issues involved in moving from US GAAP to IFRS.
• Key technical differences between US GAAP and IFRS requirements.
• Application of IFRS requirements and applicable accounting policies and disclosures.
• IFRS Measurement rules for assets, liabilities, revenues and expenses, gains and losses.
• IFRS “fair value” measurement requirements.
• Most recent IFRS standards (including financial instruments, employee benefits, business combinations, intangibles and share-based payment).
• Potential future IFRS changes and other major national accounting standards for better strategic planning.

Register online: www.haas.berkeley.edu/accounting

Day 1: Thursday, March 19
Early Adoption Challenges:
Preparation & Resource Requirements
Morning Session 8:00 am – 12:00 pm
1. Exploring pros & cons of early adoption
2. Creating an effective timeline and priorities
3. Variables and components to evaluate in Phase 1
4. Key issues in the first-time adoption of IFRS
5. Factors that enable a smooth transition
6. Key challenges of initial conversion

Instructors:
Alan Jones, Director, Transaction Services
PricewaterhouseCoopers LLP
Srijit Banerjee, Principal, Transaction Services
PricewaterhouseCoopers LLP

Afternoon Session 1:00 pm – 5:00 pm
7. An overview of key IFRS accounting policies and issues
8. Tax conversion issues
9. Process, systems and controls impacts
10. Information systems changes
11. Operational and HR needs to meet the challenges

Instructors:
Christie Simons, Partner, Accounting & Advisory
Deloitte & Touche LLP
Allfonse Upshaw, Partner, Accounting & Advisory
Deloitte & Touche LLP

Day 2: Friday, March 20
Financial Reporting Under IFRS
Morning Session 8:00 am – 12:00 pm
1. Understanding the new IFRS language
2. Impact on External Reporting
3. Elements of IFRS financial statement preparation
4. Impact on relevant ratios and numbers
5. Possible new exposures to earnings management

Instructors:
David Sawaya, Partner, Assurance & Advisory – IFRS Ernst & Young LLP
Nancy Salisbury, Partner, National Professional Practice – IFRS Ernst & Young LLP

Afternoon Session 1:00 pm – 5:00 pm
6. Recognition and measurement of assets
7. Inventories
8. Revenue recognition
9. Provisions/non-financial liabilities and other liabilities
10. Special purpose entities; Consolidated financial statements
11. Financial instruments, including the disclosure requirements in IFRS 7

Instructors:
Marcus McArdle, Partner, Professional Practice National Office, KPMG LLP
Dara Bazzano, Partner, Area Professional Practice KPMG LLP

Diploma and CPE credits will be awarded upon completion of 2-day program.
Financial Leadership Forums Taught by Haas Accounting Faculty

The California Society of CPAs in partnership with the Center for Financial Reporting and Management offered three comprehensive seminars for finance executives and high-level corporate decision-makers.

**Valuation for Mergers and Acquisitions**
Corporations continue to use mergers and acquisitions as a key strategy to stay competitive in a dynamic global marketplace. Now, however, all the rules have changed with FASB’s recent issuance of revisions for business combinations. Suneel Udpa offered a practical approach to M&A valuation with numerous real-world mini-cases to illustrate concepts and methodologies. Attendees gained insight on understanding the impact of the new rules and international convergence on business deals and gained a comprehensive and thorough understanding of accounting, tax, and valuation issues relating to M&A.

**Activity-Based Costing and Management**
Dennis Geyer offered a step-by-step system on how to design and build an activity-based cost system. Activity-based costing is a cost-modeling system based on the relationship between resources consumed in the business process and the activities that go into that process. The implications for better understanding the true costs of a company’s products or services include more strategic pricing, enhanced customer relationship management, and more effective cost reduction strategies and supplier selection, just to name only a few.

**Cost-Reduction Strategies**
In today’s competitive environment, innovation is accelerating and customers expect ever higher standards of performance. While these changes may benefit consumers by providing greater choice, lower prices and more convenience, they post enormous challenges to many businesses. Dennis Geyer talked about a new approach to cost reduction that highlights the limitations of traditional thinking. He delved into key areas such as resource planning, activity management, product design and overall system design.

Suneel Udpa

Dennis Geyer

Participants of Executive Accounting Program Class of 2008

Senior Financial Executives participating in Cost Reduction Strategies Program at Haas
Nicole Bastian Johnson joined the Haas School of Business as an Assistant Professor in 2005. Her primary areas of expertise are managerial performance measurement, incentive alignment and transfer pricing. Professor Johnson received a B.S. in Accounting and a Master's Degree in Accounting and Information Systems from Brigham Young University in 1996. She earned a Master's Degree in Statistics in 2002 and a Ph.D. in Accounting in 2005, both from Stanford University.

**Dual Transfer Pricing with Unobservable Costs**

In recent work, Professor Johnson and her co-author, Professor Thomas Pfeiffer of the University of Vienna, study the properties of dual (non-zero-sum) transfer prices using a theoretical model of a decentralized firm. In many decentralized firms, managers are given decision-making authority and are rewarded for maximizing divisional profits. In this type of organizational arrangement, transfer prices (prices assigned to internal transactions) play an important role in coordinating economic activity within the firm. For many types of transactions, however, it is difficult or impossible to find a single transfer price that aligns owners' and managers' incentives. A dual transfer price allows the buying division to pay a different transfer price than the supplying division receives for the same transaction, giving headquarters more freedom to choose prices that create optimal incentives for each division individually. Since transfer price payments are generally not cash transactions, the difference between the prices the two divisions pay is simply allocated to a corporate clearing account.

Managerial accounting textbooks often suggest that dual transfer prices can motivate managers involved in internal trade to act in the best interest of the firm when a zero-sum transfer price would fail to do so. While this may generally be true when the supplying division's costs are observable, Professors Johnson and Pfeiffer show that when the supplying division's costs are not observable and the supplying division's external market is not perfectly competitive, it becomes much more difficult to find a transfer price that motivates managers to trade efficiently, even with the flexibility of a dual transfer price. In general, motivating efficient trade is only possible when headquarters has a good understanding about the external demand faced by the two divisions. Even in this case, however, the upstream division's portion of the dual transfer price can take on a highly complex form.

Professor Johnson observes that the complexity of the optimal dual transfer price, even in this simplified setting, may partially explain why dual transfer prices are not often observed in practice.

**Other Current Projects**

Professor Johnson's other current projects include a study of abnormal stock returns following closing stock prices that fall just above or below round numbers, a study examining the performance of firms that adopt incentive compensation plans based on residual income or economic profit, and a study of the effect of round numbers in earnings-per-share announcements on announcement-period market reactions.

**2008 Haas Academic Standing**

**Undergraduate Program:**
- US News & World Report
  - #3 (Business Schools)
- Wall Street Journal
- #8 US News & World Report
- Business Week
- The Economist Intelligence Unit

**MBA Program:**
- #2 Wall Street Journal
- #8 US News & World Report
- #10 Business Week
- #6 The Economist Intelligence Unit

**Haas Alumni Network**

The Haas Alumni Network website offers alumni information and services for events, workshops, jobs and career management, chapters and groups, and volunteer opportunities. The site is also the front door to Social Media and Haas@Cal password-protected services that enable alumni to connect with each other as well as with the Haas School.

[www.haas.berkeley.edu/alumni](http://www.haas.berkeley.edu/alumni)
Haas Accounting Faculty Honored

The Big 4 Accounting Firms and Students honored the Haas Accounting Faculty at a banquet at the Bancroft Hotel on September 11, 2008. Jay Stowsky, Associate Dean of Instruction acknowledged the Faculty and thanked them for the time and effort they give to students and the professional community.

Presidents from Beta Alpha Psi, HUBBA, LBSA, and ASEND as well as Partners from each of the Big 4 Accounting firms expressed their thanks to the faculty.

Undergraduate students enjoyed opportunities to meet with CFRM Sponsors at Special Events

Representatives from Chevron, Seiler, BDO Seidman, Protiviti and California Society of CPAs each hosted tables at the Accounting Speed Networking Night.

Recruiters from BDO Seidman, Blanding Boyer & Rockwell, Seiler, and Protiviti discuss internship opportunities with students at Finance and Accounting Internship Reception.

Students learn about scholarship opportunities from Soco Davenport of the California Society of CPAs.
CFRM invites accounting professionals to speak to students and bring their real-world experiences into the classroom to further enhance Haas’ curriculum.

**Career Panels**

**UGBA 121 Federal Income Tax Accounting**
Alan Cerf  
Ting Ba, Tax, Burr, Pilger & Mayer LLP  
Pamela A. Dennett, Senior Director, BDO Seidman LLP  
Mathew Urbina, Tax Services, Ernst & Young LLP  
Lawrence P. Varellas, National Managing Partner, Deloitte Tax LLP  
Kent F. Wisner, Principal, KPMG  
Paul Reshke, Tax, PricewaterhouseCoopers LLP  
Matthew Nadboralski, Manager, Seiler LLP

**UGBA 102A Introduction to Financial Accounting**
Rada Brooks and Dennis Geyer  
Ed Kennedy, Partner, Ernst & Young LLP  
Tiffany Rasmussen, Audit Partner, KPMG LLP  
Tom Francis, Audit Partner, Deloitte & Touche LLP  
Kristin Rivera, Partner, PricewaterhouseCoopers LLP

**UGBA 121 Federal Income Tax Accounting**
Alan Cerf  
Christine Liang, Manager Tax, Financial Services Office, Ernst & Young LLP  
Warren Glettner, Tax Partner, PricewaterhouseCoopers LLP  
Nancy Young, Senior Manager, Seiler LLP  
Larry Varellas, Tax Partner, Deloitte LLP  
Philip Mogen, Tax Partner, KPMG LLP

**Key Financial Executives Invited to Dean’s Roundtable Discussions**

Former Dean Tom Campbell and CFRM Executive Director Solomon Darwin hosted three roundtable discussions for key financial executives. The lunch discussions provide an informal, small-group setting where executives can exchange ideas and discuss issues of common interest. Dean Rich Lyons plans to continue the luncheons, with the next one being held on December 11th.

**This past year’s guests included:**
Christina Cook, Bank of Marin  
Ernest J. Furtado, Textainer  
Michele Iversen, Washington Mutual Bank  
Kenneth Lewis, Franklin Templeton Investments  
Steve McCann, Longs Drug Stores  
Sharon McCollam, Williams Sonoma  
Maria Nondorf, Haas School of Business  
Pat Persse, CompWest Insurance Company  
Byron Pollitt, Visa  
Mike Ray, California Casualty Management Co.  
Ed Scheuer, Protiviti  
Hans Ploos van Amstel, Levi Strauss  
Bob Walker, Financial Executives International  
Jim Wall, Financial Executives International  
Angela Yip, San Jose Water Company
**Guest Speakers in the Classroom**

**UGBA 120A Intermediate Financial Accounting**  
Vic Stanton  
Dara Bazzano, Partner, KPMG LLP  
Fain McDaniel, Partner, KPMG LLP  
Discussion: Current impact and status of IFRS in accounting education in the profession.

**UGBA 122 Financial Information Analysis**  
Vic Stanton  
Jim Turner, Director, Consulting Group, BDO Seidman LLP  
Discussion: Subprime meltdown and current bailout plan and how it impacts consulting.

**UGBA 127 Strategic Cost Management**  
Rada Brooks  
David Deming, Manager, Bain & Company  
Discussion: Evaluating and managing customer profitability and relationships.

Stan Hales, Partner, PricewaterhouseCoopers  
Discussion: Issues and latest developments in transfer pricing.

Miles Ewing, Partner, Deloitte & Touche  
Discussion: Best practices in structuring corporate performance evaluation systems.

**Big 4 Judged Student Presentations**

**UGBA 127 Forensic Accounting**  
Solomon Darwin  
Mark E. McComb, Partner, KPMG LLP  
Jim Meehan, Partner, PricewaterhouseCoopers LLP  
Sam Parish, Sr Manager, Forensic Practice, Deloitte LLP  
Carlos Singh, Sr Manager, Fraud Investigation & Dispute Services, Ernst & Young LLP  
Discussion: Big 4 partners and managers judged student presentations on accounting fraud in various companies.

**EW MBA 202 Financial Reporting**  
Solomon Darwin  
Doug Aguilera, Sr. Manager, Ernst & Young LLP  
Sydney Firestone, Dispute Director, Deloitte LLP  
Gerry Fujimoto, Partner, Deloitte LLP  
Warren Glettner, Partner, PricewaterhouseCoopers LLP  
Linda Justice, Dispute Sr. Manager, Deloitte LLP  
Jennifer Lindsay, Forensic Partner, KPMG LLP  
Alexander Marcal, Partner, Deloitte LLP  
Jeff Rhodes, Director, KPMG LLP  
Heather Van de Velde, Sr. Manager, Ernst & Young LLP  
Gary Waldock, Director, PricewaterhouseCoopers LLP  
Discussion: Big 4 partners and managers judged student presentations on financial reporting projects.
Letter from the President of Beta Alpha Psi

At the heart of Beta Alpha Psi is a passion that resonates in each of our members to push our academic, professional, and personal development beyond what a traditional undergraduate education offers. As the premier honors business fraternity, Beta Alpha Psi is internationally recognized for academic and professional excellence. The Lambda Chapter, established in 1925, continues this legacy as a Walter A. Haas sponsored business fraternity at the University of California, Berkeley.

This semester will be no exception to our tradition of excellence as a Superior Chapter in the Western Region. Not only are we starting off the semester with fond memories of winning the 2008 Cisco-Deloitte Case Competition (Haas Sponsored Internal Case Competition), but our recent co-sponsorship of the Big Four Forum and PricewaterhouseCoopers Interview Workshop are just a few more examples of how Beta Alpha Psi bridges the gap between students and the opportunities available in financial services and beyond.

Beta Alpha Psi prides itself as the number one student organization for case competitions at Cal. We have historically won numerous internal case competitions over the past several years, enabling our brothers to travel abroad and represent both our university and fraternity. Over the past academic year alone, Beta Alpha Psi has won or received a finalist position in the Copenhagen Business School Case Competition (Denmark), Goldman Sachs Investment Banking Case Competition, the Cisco-Deloitte E-Business Case Competition, the Deloitte Financial Advisory Services Case Competition, the IBM Case Competition and the Citi International Case Competition (HKUST).

Yet it is only through the continual dedication of Solomon Darwin, our Faculty Advisor, and the unwavering support of our alumni, faculty, and countless professionals that we are able to offer such rich opportunities and quality events to our members and the community. With that in mind, we welcome your ideas for possible events or partnerships. Please feel free to email me at sgupta@berkeleybap.org.

It has been my greatest pleasure to be part of such a dynamic organization for the past two years. With so much external support and the passion for business I see reflected in each of our members, I’m confident that Beta Alpha Psi will continue to push the boundaries of what an undergraduate education beyond the classroom means here at UC Berkeley.

Warm Regards,
Sagar Gupta
President, Lambda Chapter

Beta Alpha Psi Awards and Achievements

- Recognized as Superior Chapter in the Western Region
- Awarded $50,000 by KPMG for maintaining Superior Status
- Copenhagen Business School Case Competition (Denmark)
- Goldman Sachs Investment Banking Case Competition
- Cisco-Deloitte E-Business Case Competition
- Deloitte Financial Advisory Services Case Competition
- IBM Case Competition
- 2007 Citi International Case Competition

Congratulations to the L.H. Penny Grant-In-Aid Fund award recipients for 2008-2009:

Reilly Grellas
Jeffrey Kwong
Robert Kaiser
Students Shine in Case Competition

Haas Team Wins 2008 Citi International Case Competition in Hong Kong

Eighteen universities from around the world participated in the 2008 Citi International Case Competition (CICC) on October 27 at the Hong Kong University of Science and Technology. The case company was Ocean Park, a popular amusement park in Hong Kong undergoing major redevelopment and expansion. Judges on the panel included Ocean Park’s CEO, VP Sales and Marketing, the head of Citi Global Markets Banking in HK, HKUST business professors, and other top executives from Citi and Ocean Park. Each team had 26 hours to conduct an in-depth analysis of the case and provide strategic recommendations to Ocean Park management.

The Haas School team consisted of Sean Huang and Wei Li, both BS 09, and Sagar Gupta and Jimmy Shi, both BS 10. Sagar Gupta also received the “best presenter award”. Janet Amador, the Haas Undergraduate Program’s director of admissions and operations, was their advisor.

This is a tremendous milestone for both Beta Alpha Psi and Haas School of Business, as this is the first time Haas has won an international case competition in 10 years.

The Citi International Case Competition is sponsored by the Citi Foundation and jointly organized by Citi and the HKUST’s School of Business and Management.

Haas Undergraduate Team Wins PricewaterhouseCoopers Case Competition

A team of Haas undergraduates won the top prize in the PricewaterhouseCoopers’ annual xACT (extreme accounting) Campus Competition, a challenge that gives students exposure to real world accounting and auditing issues.

Haas School undergraduates Milan Agarwal, Stephanie Chien, and Davis Liu, along with UC Berkeley sophomores Christina Ting and Cailin Trinh comprised the winning team, beating out finalists from the University of Texas, the University of Illinois, Wake Forest University, and Louisiana State University. They were one of five teams out of approximately 350 teams in the United States selected to compete in the finals in New York. As a finalist team, the Berkeley students won $10,000 and a trip to New York City for the January 18 competition finals. While in New York, the team met with experts from Pricewaterhouse-Coopers’ Risk and Quality Group to learn how accounting and auditing positions are developed.

The competition was designed by Pricewaterhouse-Coopers’ Risk & Quality practice to present challenges that focus on the impact of accounting policy on the business and investing community. Finalists presented their solutions to a panel of Pricewaterhouse-Coopers partners and leaders. “The Haas team demonstrated great team work,” says Rada Brooks, Haas faculty member and team advisor. “The students were particularly impressive in their focus on the overall strategic objective of the case.”
Undergraduates Compete in Case Challenge in Arizona

Having won the opening round of the Deloitte Financial Advisory Services Case Challenge, a team of Haas undergraduate students traveled to the competition’s six-team national finals in Scottsdale, Ariz., April 5 and 6.

The winning team consisted of Miranda Wong, BS 09; Nicole Hui, BS 09 (economics); Andy Lau, BS 09; and Michelle Wu, BS 09. The team earned its spot in the final competition for its proposal on how to time a 100-employee layoff in order to minimize the impact on a company’s year-end finances. The first-round competition was held March 7 at Deloitte’s San Francisco office.

The final round required the teams to develop a model for evaluating the fair market value of a company based on its assets and liabilities. The Haas students competed against teams from Brigham Young University, University of Connecticut, University of Illinois, Morehouse College, and University of Notre Dame. Each member of the first-place team will receive a $2,000 scholarship, while members of the runner-up team will be awarded a $1,000 scholarship. The winning team also earns $10,000 for its school, while the runner-up team wins $5,000 for its school.

Undergraduates Best Stanford, San Jose State in Case Competition

For the second year in a row, Haas undergraduates defeated Stanford and San Jose State universities to take first place at the annual Deloitte-Cisco “Battle of the Bay” Case Competition, held at Cisco Systems on March 14.

The winning team members were Sean Huang, BS 09; Sagar Gupta, BS 10; Wei Li, BS (economics) 09; and Jimmy Shi, BS 10.

To qualify for the “Battle of the Bay” competition, the Haas group competed in and won the eBusiness Case Competition sponsored by Cisco Systems and Deloitte Consulting at the Haas School earlier this spring. Both competitions asked students to create a go-to-market solution for a newly developed software product by Cisco called the Entertainment Operating System (EOS).

The Haas team impressed Deloitte and Cisco executives with its marketing theme and pricing strategy. Students recommended that Cisco strengthen its position in the consumer market by applying its existing “Welcome to the Human Network” marketing campaign to EOS and eliminating licensing fees to focus on generating revenues through ad sharing and content hosting.

Judges gave team members high marks for the caliber of their presentation skills, professionalism, and ability to respond thoroughly and knowledgeably during the question-and-answer session.

To become members of the National Honors Business Fraternity Beta Alpha Psi, the Haas students completed an intensive 10-week pledging process, which consisted of professional development, business education, and presentation training. “As a result, we were adequately equipped with business skills that helped distinguish our group and win this case competition,” says team member Gupta.

ALPHA/KPMG/DELOITTE Case Competition

Over 30 teams from Universities in the United States competed in the national ALPHA/KPMG/Deolette case competition. The Haas team was composed of Jose Padilla, Brittany Bianchi, Isela Arias, Robert Perez and Elizabeth Padilla, who made it to the finals in the four day competition, and were one of the runners up. Vic Stanton was the Berkeley team advisor.
Welcome New Accounting Phds

HARM SCHUETT
Harm Schuett, from Germany, received his diploma (equivalent to a master) at the Ruhr-Universität Bochum in Germany in 2007 with specializations in Accounting, Econometrics and Marketing. He worked for Sal. Oppenheim – Europe’s largest private bank – as a sell-side financial analyst for one year. He was part of the analyst team covering industrial goods and services companies. His research interests are directly influenced by his experience as an analyst and evolve around accounting quality and its link to market participant’s actions. Harm says he wanted to pursue a PhD in accounting to contribute to “the most important debate of our times; the debate on how to shape a modern market system.”

YUAN (ESTELLE) SUN
Yuan (Estelle) Sun, originally from China, received her bachelor’s degree with first class honors in accounting at the University of Otago, New Zealand in 2006. In 2007-2008, she taught intermediate financial accounting courses in the Department of Accountancy and Business Law at Otago.

Her research interests focus on two fields: the economics of accounting and auditing, and capital market research. In particular, she is interested in the areas of contracting relationship, earning management and their interactions with corporate governance and auditing. She is also interested in investigating how investors respond to managers, company boards, and auditors’ decisions, and the role of accounting information in capital market by undertaking capital market research.

AYDIN UYSAL
Aydin Uysal, originally from Turkey, has lived in San Francisco for nine years. He earned his BS in Operations Research from Bosphorus University, Istanbul Turkey in July 1999 and MBA from Golden Gate University in San Francisco in 2001.

He worked as a quantitative analyst at Moody’s KMV for five years, Quantal Asset Management for one year, and Barclays Global Investors for two years.

His research interests are in capital markets and predictability of stock returns through macro variables and financial statement information. He enjoys reading and book binding.

Accounting Professor Qintao Fan Receives The Earl F. Cheit Award for Excellence in Teaching for the PhD Program

PROFESSOR QINTAO FAN
At Haas, excellence in teaching is recognized through the annual Earl F. Cheit Award. This award is named after Dean Emeritus Earl F. Cheit, who made teaching excellence one of his top priorities as dean. The recipients of the Cheit Award are chosen by panels of students based on nominations submitted by students.

Professor Qintao Fan was selected as the 2008 recipient for the Ph.D. Program. Qintao joined the Haas School of Business in July 2003. She holds an MA in Economics from the University of Maryland at College Park, an MS in Statistics and a PhD in Business Administration from Stanford University.
Darwin: US GAAP – has long served as the Gold Standard for the Western Capital Markets. Without the US GAAP for benchmarking, financial reporting may quickly decline to the lowest common denominator. Can IFRS flourish if US GAAP is dead?

Herz: Thanks for the compliment about GAAP. It’s good, and when supplemented by SEC requirements, it generally leads to good reporting. But that’s not to say other parts of the world aren’t doing a good job also. And a key aspect of the Memorandum of Understanding (MoU) relates to developing improved standards. Through our work with IASB we can inject the best of US “GAAP Genes” into the DNA of IFRS including thorough, open due process and an investor focus. The IASB will also need an appropriate amount of secure funding and adequate staffing to achieve its goals. Both boards and our Trustees are very cognizant of these things.

Darwin: Academic Research

Strongly suggests that GAAP is superior to IFRS based on Professor Teri Yohn’s testimony to the US Congress on October 24, 2007. Professor Yohn of Indiana University, brought to bear about 25 high-quality academic research studies that indicate that investors appear to prefer US GAAP over IFRS, and that IFRS has provided greater opportunities for earnings management. Are we acting in the best interest of the investment community by taking this new direction?

Tweedie: Neither system is perfect and each has its strengths. That is why our convergence efforts seek to identify the best answers from each set of standards. Where neither has an answer that is considered to be of sufficient quality, the two boards work together to write a new standard. Our shared goal is that by 2011 we will have an enhanced set of IFRSs, derived from the best of US GAAP and existing IFRSs.

Herz: I agree with David and would add that most investors strongly support the goal of creating a single set of high quality standards – with strong auditing and strong regulation and enforcement married with it. The key is focusing on the “high quality” part of that goal. The MoU represents and speaks to the projects where both sets of standards need to be improved.

Darwin: What will be the Cost benefits of IFRS? There seems to be a general feeling that this is another SOX 404 waiting to happen. First, there will be the costs of conversion followed by the costs of implementation and perhaps the cost of establishing a lofty internal control system. This may run into billions of dollars, for new “services” like training, systems reengineering and whatever else companies need to pay for. The politically correct answer is that conversion to IFRS will reduce the cost of capital by achieving comparability through principles-based standards. Is there evidence that IFRS will reduce the cost of capital, much less be able to cover the humongous costs of conversion?

Herz: Academic research has indicated that there have been benefits in terms of lowering the cost of capital to companies switching from their national GAAPs to IFRS. But that has related to countries that arguably had a less robust reporting regime than either IFRS or US GAAP. While I am not aware of any such research having yet been done relating to a future switch from US GAAP to IFRS, I personally believe that a switch to a single set of high quality international standards would reduce the cost of capital to US companies. Just the ability to compare companies in the same industry – in different global locations – will be more direct, easier for investors, and will add greater clarity and efficiency to the investment process. Additionally, recent trends suggest that more and more of the world’s capital will come from countries outside the US. For sure, there will be significant upfront costs – but I think there will be a payback later. Further, for global companies, there will be operational efficiencies by utilizing a single set of standards across their international operations for reporting purposes.

Darwin: The evolution of US GAAP is a response to the need for specific rules in order to deter management’s self-interest in the reported earnings and financial position. It is much easier to hide behind principles than rules. Policing will be difficult when there are no rules; confusion and disputes among related parties may result in increased litigation. Do you think IFRS once implemented system-wide will result in more litigation in the US?

Herz: Actually, strong principles rooted in strong concepts can produce better reporting. Too many rules can undermine professionalism in the preparation and auditing of financial reports, can promote false comparability and form over substance structuring, and can impede effective communication between companies and investors. Furthermore, I’ve heard some eminent attorneys state that in their view it will be more difficult to prove a case that is tied to a principles-based system. So, it’s unclear whether a move to a more principles-based system would increase or reduce the amount of litigation.

Darwin: The FASB concluded in 1999, based on its extensive report on the similarities and differences between IFRS (IAS at the time) and US GAAP that IFRS was lower quality than GAAP. What has changed during this time to close the gap between the two GAAPs?
Herz: We’ve done lots of work together with the IASB to close gaps and to develop common, improved standards – and we have lots more to do as well in connection with the MoU. That’s the key – to jointly create improved standards in major areas. In this way we are reshaping both US GAAP and IFRS into a common set of high quality standards.

Darwin: If It Ain’t Broke, Don’t Fix It! US GAAP for the most part has resulted in incremental improvements, though far from perfect, it evolved over time based on experience in our capital markets, it works and is not broken. Why fix it?

Herz: The MoU acknowledges that in very important areas current financial reporting is not giving investors all the information they need. For example, investors routinely adjust financial statements to capitalize operating leases. That’s a signal that the current standards aren’t doing their job. Our advisory groups, which include investors, have confirmed that we have the right priorities and the right projects as part of the MoU and that successfully completing these would represent needed improvements in accounting standards.

Darwin: Preparers, auditors and investors will need to learn to produce or interpret a new kind of financial statement. Professors will need to learn to teach IFRS; students will need new books. One industry that will certainly thrive on the use of IFRS in the US is training, education and certification. All sorts of certification programs will need to be revamped, including state CPA requirements. Who will coordinate this effort to match the timing between the needs with resources for implementation?

Herz: I believe we need a national plan or blueprint that identifies all the issues and who should tackle them and how they should be tackled. In this way we can help ensure an orderly transition to IFRS that provides sufficient lead time to properly address education, training, and certification. As I’ve said previously, a large number of the differences and areas of overlap and the cross referencing that existed between the various documents that previously comprised the US authoritative literature. Further, as we progress with the MoU, we will be replacing existing US GAAP with the new jointly created standards. Thus, subjects like Revenue Recognition, where current US GAAP is comprised of over 200 different pronouncements will be replaced by a single standard, probably supported by appropriate application guidance. But I think your point is valid in that in other areas, US GAAP may remain a source of helpful implementation guidance, providing that guidance doesn’t conflict with IFRS.

Darwin: Research by accounting analyst Jack T. Ciesielski took a small sampling of financial statements prepared under IFRS and GAAP and found disturbing differences. Out of 20 statements, 10 showed lower earnings under IFRS while the other 10 showed the opposite. One IFRS statement showed earnings 41.3 percent over GAAP, while another showed GAAP reporting 336.6 percent more than IFRS. One showed equity 83.4 percent higher under IFRS, while another had GAAP reporting 98.7 percent more. As this requires considerable education and knowledge, are the American investors prepared for the task?

Herz: That study was prepared under existing standards. As I’ve said previously, a large number of the differences will go away as we complete the projects on our MoU. Whether the adoption of this improved IFRS would then increase or decrease reported earnings will likely be company specific, depending on the underlying facts and circumstances. But certainly, all of this will represent significant change and that’s why it needs to be done in an orderly way that provides adequate lead time for all the education and training that will be needed.

Darwin: Has Fair Value accounting contributed to the current financial crisis?

Tweedie: No. All that fair value has done is describe the economic position of a company. Recent reports have indicated that the total losses on mortgage-backed securities
are estimated to be in the region of $1.2 trillion, yet only $500 billion is publicly disclosed so far. That leaves around $700 billion of losses yet to be reported. No one knows where the remaining undisclosed losses are sitting, so what you have is credit markets that have seized up because of a complete lack of confidence in counterparties. The only way to deal with this is to provide more transparency, not less. Fair value is not perfect but it does seek to uncover the true economic position.

This was the problem Japan had during the ‘lost decade’ of the 90s. No one believed the numbers being reported by Japanese banks, so the problems were never dealt with. In a recent interview Mr Watanabe, the Japanese Minister of Finance, said that ‘the right tools were needed to establish the true value of assets rather than [doing what Japan did and] avoiding ever facing up to the problems. What we need right now is more transparency, not less. Investors fear uncertainty. Confidence will only be restored when investors and counterparties believe in the numbers.

Herz: I agree with David. Fair Value has reflected the current reality and helped to shine the spotlight on problems at particular institutions. It’s grounded in economic reality. Accountability requires honest accounting and informative disclosure, even when the news is bad.

Unfortunately, as we have seen in the past – and in some instances during the current crisis—some corporate executives try to manage the story through accounting, particularly when there is bad news or to try to cloak the effect of their bad decisions. And when complying with a particular standard would present a less flattering picture than desired, some folks may employ a “shoot the messenger” tactic of blaming the accounting requirements or the auditors rather than owning up to their prior poor business decisions and faltering financial condition.

Darwin: US GAAP operates under the oversight of the US Congress, SEC and FASB. Given the lack of sovereignty over IFRS, there is a real risk of near total loss of US influence over accounting standards. How and from where will IFRS attain empowerment and authority as we move forward? Do we run into the risk of not having a single legal authority for representation?

Tweedie: Firstly, the SEC will continue to retain responsibility for accounting standards in the US, regardless of whether they are IFRSs or US GAAP. The IASB has no authority to impose its standards on any country. New or revised IFRSs must first go through a local endorsement process managed by the local standard-setter and overseen by the regulator. The situation in the US would be no different.

Secondly, US interests are well represented at all levels of the IASB and our oversight body, the IASC Foundation. Around a quarter of Trustees and members of the IASB come from North America. The IASB structure was originally modelled on that of the FASB.

And finally, the Trustees of the IASC Foundation, our equivalent of the Financial Accounting Foundation (FAF), have published proposals to establish a formal link between the organisation and a Monitoring Group comprising representatives of public authorities (including the SEC) and international organisations that have requirements for accountability to public authorities. The Monitoring Group would be responsible for approving Trustee appointments and ensuring that the Trustees adequately discharge their oversight responsibilities.

Darwin: The US SEC will continue to be very active in enforcing Accounting Standards. If other regulators around the world are not as active in enforcement, will there be an inconsistent application of IFRS?

Tweedie: You are right to highlight that some countries have claimed IFRS-compliance, yet have either failed to adopt the full set of standards or been less vigorous in their enforcement. This is an issue that our Trustees and securities regulators internationally are taking very seriously.

US leadership in this area is very much appreciated. The SEC very helpfully insisted that only foreign issuers reporting under full IFRSs as issued by the IASB can avoid reconciling to US GAAP. IOSCO has also recently issued guidance on the disclosure of reporting frameworks used in compiling financial statements.

Darwin: In a dispersed corporate ownership that is dominant in the US, stock price has a significant effect on executive compensation – a stimuli to manipulate accounting earnings. Top executives of public companies may favor IFRS because it will be easier to make their numbers. Accounting rules should make it difficult to manipulate earnings. Academic research concludes that IFRS is less rigorously applied than US GAAP. How does IFRS help safeguard the investor?

Tweedie: I do not agree that IFRSs are less vigorously applied, but it is fair to say that by adopting principle-based standards that require judgement to be applied you may end up with a small range of answers to the same question. US GAAP and IFRSs are both based on high quality accounting principles – it’s just that in the US there are thousands of pages that tell you how to apply them. As a result it is becoming impossible to conduct an audit of a large organisation without a roomful of technical experts just in case something on page 10,256 has been missed. That cannot be right. Accounting is not rocket science. There is little point in universities producing highly trained and qualified accountants if they are going to be treated like workers on a production line.

Darwin: IFRS-style accounting would be a gift to US managers, as outright fraud is better identified under rule based accounting rather than IFRS principle based accounting. Will IFRS create room for a more subtle means of “earnings management.”
Tweedie: I absolutely disagree. A well crafted principle will catch more fraud than a 10,000-page rulebook. Those who wish to commit fraud will often find a way around rules. Defeating a principle is a great deal harder.

Darwin: IFRS may work in 100 or so countries where capital markets are not well established. How can we be certain that it will work in the US environment? Isn’t it like removing all the traffic signs in the US where we have well established and extensive freeway systems?

Tweedie: Almost every major capital market in the world now permits, requires or is in the process of converging with IFRSs. Those already requiring its use include Australia, France, Germany, Hong Kong, South Africa and the UK, with Canada, India, Japan and Korea all adopting or converging with IFRSs by 2011. And as a result of the MoU agreed between the IASB and FASB in 2006 the underlying principles within US GAAP and IFRSs are likely to be substantially the same by the time the MoU is completed in 2011.

Darwin: Last month, The UK-based Association of Investment Companies (AIC) issued a statement urging that investor viewpoint should be placed at the heart of new standards and that the work of IASB is somewhat lacking in this area. Is the investor viewpoint ignored under the IFRS? Are effective mechanisms in place in the IFRS due process? Are they working?

Tweedie: Getting well qualified investors onto standard-setting boards is a problem for us all – both at the IASB and the FASB. But we’ve made good progress in the last year or so. In August last year, Stephen Cooper joined the IASB. As an analyst, Stephen is recognised as a leader in his field. In each of the last ten surveys, he has been voted top European Valuation and Accounting Analyst by Extel and Institutional Investor Magazine. We continue to seek others with an investment background to join the staff and board of the IASB.

Darwin: International Organization of Securities Commissions (IOSCO) appears to play a similar role in some aspects to that of the SEC in the EU. This is an organization that does not have any teeth at the present time. Do you see IOSCO playing a key role in the future? If so, from where will it get its teeth?

Tweedie: IOSCO is an international group of securities regulators that includes the SEC. Securities regulators in Europe are represented by the Committee of European Securities Regulators (CESR). Investors operate across international markets, increasingly using IFRSs, making it appropriate that there is greater co-ordination amongst securities regulators globally.

Darwin: George Washington University Law professor, Lawrence A. Cunningham, noted cases of EU members ignoring EU directives, Italy and France exercising national sovereignty to resist corporate takeovers and various countries establishing their own national version of IFRS. What controls are in place to apply global accounting standards uniformly?

Tweedie: From the US angle, any foreign company seeking to list in the US has to report on the basis of IFRSs as issued by the IASB. Globally, widespread adoption of IFRSs is a market-driven phenomenon. The IASB has no power to mandate countries to adopt our standards uniformly. However, what we have seen is that countries that cherry-pick or adapt standards to meet local requirements are punished by the market. They take on the pain of transition without the gain of recognition.

Darwin: Does IASB plan to utilize the knowledge base of the US GAAP in the future development of IFRS?

Tweedie: Absolutely, we have done so over the last five years whilst seeking convergence in our standards.

Darwin: US GAAP started out as principles based, as denoted by the “P” in GAAP. Over time it evolved into a rule based Accounting System for good reasons. To give you an analogy, when the first Model T rolled off the assembly line, there were no Traffic Rules then. As we built more roads and freeways, over time the infrastructure demanded more rules to protect and safeguard its citizens from accidents as well as to promote an efficient flow of traffic to benefit the community as a whole. Given that experience, will the IFRS turn into a rule based Accounting System over time?

Tweedie: To build on your analogy, if you gave all car drivers a 20,000-page instruction manual, would they read it? Herein lies the problem. It is unrealistic to expect such a system to work efficiently. The financial crisis is due in part to investors not fully appreciating the underlying risks of what they are buying. The Interpretations Committee of the IASB (IFRIC) works hard to avoid layering on enormous amounts of guidance, and the profession has needed to get used to not having all of its questions answered. Professional judgement has to be applied.
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