

Transaction Complexity and the Movement to Fair Value Accounting

Pinky Rusli – Montana State University

Xinlei Zhao, and David A. Ziebart – University of Kentucky

business transactions are becoming more complicated and complex

- Do accounting standards reflect differences in the complexity of the transactions being recorded?
- Does the use of mark-to-market (i.e., fair value) accounting reduce the complexity of standards by relying on market valuations to capture transaction complexity?
- Does the reliance on fair value measurements reduce audit costs for transactions with significant complexity

Since accounting is a human contrived system, accountancy theory and practice are determined by consensus regarding

- *what* is to be measured
- *when* it is to be measured (recognized or derecognized)
- *how* it is measured
- *who* is the entity for which the accounting occurs
- *where* the element or activity takes place.

complexity in the underlying transactions is manifested in the complexity of the authoritative guidance (standards)

- Our investigation draws upon a fundamental notion that control mechanisms, including accounting regulation, require a more complex mechanism than the process or activity being controlled. Our findings support this argument.

an economic consequence of accounting complexity

- an audit fee premium is placed on complex transactions.
- the use of fair values (reliance on observed market values) is more cost effective than overly complex accounting standards to cope with the increase in transaction complexity