What is GAAP?

Worksheet

GAAP is the standardized framework of accounting rules and conventions — including principles like consistency, materiality and going concern — that publicly traded U.S. companies must use to prepare financial statements.

Questions

1. GAAP is primarily used by companies in which country/region?

A) United States
B) European Union
C) Japan only
D) Global — identical everywhere

2. Which organization sets GAAP?

A) IASB
B) SEC directly
C) FASB
D) IRS

3. GAAP is best described as:

A) A single universal law
B) A tax code
C) A framework of accounting rules and standards
D) A stock exchange requirement only for banks

4. Compared to IFRS, GAAP is generally:

A) More principles-based
B) More rules-based and detailed
C) Identical in every rule
D) Only used for tax filings

5. A company changes its depreciation method from straight-line to declining balance. Under GAAP, what must it do?

6. A retailer's revenue is 50 million and it just received a2,000 vendor rebate. Should it be highlighted as a separate line item?

7. A manufacturer buys a $120,000 machine with a 10-year useful life and no salvage value. How does GAAP require the cost to be recognized?

8. Define: What does GAAP stand for?

9. Define: Who sets GAAP in the United States?

10. Define: Why does GAAP exist?

Answer Key

1. A) United States — GAAP is the U.S. accounting framework, set by FASB; most other countries use IFRS.

2. C) FASB — The Financial Accounting Standards Board (FASB) establishes and updates GAAP.

3. C) A framework of accounting rules and standards — GAAP is a comprehensive framework of principles, standards and procedures for financial reporting.

4. B) More rules-based and detailed — GAAP tends to give very specific, detailed rules, while IFRS relies more on broad principles and judgment.

5. Identify the change as a change in accounting estimate (or principle) Disclose the nature of and reason for the change in the notes Apply the new method prospectively (going forward), not retroactively Ensure comparability is preserved through disclosure, per the consistency principle

6. Compare the rebate (2,000) to total revenue (50,000,000) = 0.004% Because it is far below common materiality thresholds (often 0.5%–5%) GAAP's materiality principle says it can be grouped with other income No separate disclosure is required

7. Apply the matching principle: match the expense to the revenue it helps generate Spread the cost over the useful life instead of expensing it all at purchase Annual depreciation = 120,000 / 10 =12,000 per year Record $12,000 depreciation expense each year for 10 years

8. Generally Accepted Accounting Principles — the standard U.S. framework for financial reporting.

9. The Financial Accounting Standards Board (FASB).

10. To make financial statements consistent, comparable and reliable across companies.