

ACCT 742
Problems in Financial Reporting
Spring 2010 SYLLABUS -- Preliminary

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Course Overview

Financial statements are a primary means for firms to communicate information about their performance and strategy to investors and other groups. In the wake of numerous accounting scandals and the recent financial meltdown (which accounting both helped and hindered), it is more important than ever for managers and investors to understand (i) the financial reporting process, (ii) what financial statements do and do not contain, and (iii) the types of discretion managers have in presenting transactions they have undertaken. This course is designed to help you become a more informed user of accounting numbers by increasing your ability to extract, interpret, and analyze information in financial statements.

We will focus on many of the biggest problem areas of financial reporting:

- Earnings and Cash Flow Quality
- Earnings per share and Alternative Measures of Performance
- Revenue Recognition
- Securitizations
- Fair Value and Mark to Market
- Derivatives
- Stock Options
- Pensions
- Consolidation of Debt and “Off Balance Sheet” Debt
- Special Purpose Entities variable Interest Entities and Control
- The Financial Reporting Environment Post Enron
 - Sarbanes-Oxley Law
- International Standards

While this is not a course in equity valuation *per se*, equity valuation is one of the most common uses of financial statement data. Accordingly, we will examine the relation between stock prices and financial statement information. We will spend time on financial statement analysis, ratios, and forecasting.

The course assumes a solid understanding of basic financial accounting (at the level of Acct 620/621).

Course Materials

Bulk pack The bulk pack is being developed. All of the material will be available in the eRoom for Acct 742 on Web Café.

Text: Revsine, Collins, Johnson, Mittelstaedt, *Financial Reporting and Analysis*, 4th ed., Prentice Hall, 2009.

Web Café The course has a room on Web Café that you can log onto with your User name and Password. Within the Course Material folder, there is a folder for each class session, as well as one for the syllabus and the exams. Inside the folder for a given class session, you will see three or four subfolders:

Bulk Pack Material: This includes notes, problems, cases, and readings that were included in the bulk pack.

Pre Class Material: New readings, problems, and cases (ones not included in the course pack) are contained here. This folder will also have any spreadsheets available to help work the problems and cases. Finally, this folder will contain power point slides that will constitute the outline of what we'll cover in class that day. The slides will be printed out for you and distributed at the beginning of class.

Solutions and Post Class Material: This is where I'll post solutions, corrections, etc

Office Hours

Feel free to call with questions or contact me via email at the address above. E-mail is often an easier and quicker way to get your questions answered.

Grading and Course Requirements

Your grade for the course will be determined on the basis of:

Class Participation	20 %
Individually Done Case Write Ups	20 %
Course Project (group)	30 %
Exams	<u>30 %</u>
Total	100 %

Class Participation

The amount of learning that takes place in the course will depend on how active the class discussions are, which is dependent on the amount of preparation you do before class. Class participation will be based on your contribution to the class discussions and analyses, not simply on the amount of time you talk. If necessary, I will cold call students.

Because entering or leaving the classroom during class time is disruptive to the learning environment, your fellow classmates and I expect that you will not do so, except in an emergency.

Please bring to each class a Name Card, with your name printed in **LARGE DARK LETTERS**. This will facilitate my getting to know your names and my ability to reward you for class participation.

INDIVIDUALLY DONE Case Write Ups:

Each student is required to write-up answers to 3 of the cases we will be covering in class.

If you want to hand in answers to more than 3, I will count the 3 best cases. Cases must be handed in the day before the class session. Cases will be graded on the basis of effort and completion along with accuracy. Cases are to be done INDIVIDUALLY.

Course Project:

Students are asked to form groups of up to 4. Groups should be finalized and your company choice made by the sixth class meetings (February 2). The earlier you decide on a company, the more time you'll have to work on it.

Each group is expected to turn in the Course project on the last day of class. In addition to submitting a written assignment for the project, group members will be expected to prepare a brief presentation of their findings. We will do the presentations during class.

Your group must identify a firm that has been the subject of an accounting controversy (alleged or real). you can use internet search engines to help you pick your firm, SEC actions, etc. Choose a firm and accounting issue you are interested in. Be sure that the issue your group tackles has a significant element of accounting judgment. Putting the wrong date on a sales contract or an option grant (i.e., backdating) is simply fraud, not an accounting judgment issue.

Please do not choose Enron, Sunbeam, WorldCom, Microstrategy, or AOL. Moreover, do not choose any firm and their accounting controversy that we will be covering in class.

Once you have identified a firm and its accounting controversy, send me an email letting me know who and what you've selected. I would like to approve the selection before you begin.

More details will be provided during class and on the course web page.

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Group Project Assignment

First, find a company that has been criticized or investigated for some questionable *accounting practice*.

- Good places to search include popular press articles, analysts reports, or the SEC accounting enforcement page (<http://www.sec.gov/divisions/enforce/friactions.shtml>)
- Do *not* choose Enron, WorldCom, AOL, Sunbeam, or Micro strategy.
- Make sure that you choose a firm with questions about its accounting practices rather than a firm that has committed outright fraud. For example, a firm that ships empty boxes and books revenue is a fraud. A firm that ships actual product and books all of the revenue without any provision for bad debts has questionable accounting practices.
- The degree of difficulty will be taken in account in grading your project. For example, if you investigate a firm with questionable pension accounting practices, which we will not cover in class until after the assignment is due, you will be given more slack in grading than if you investigate a simple revenue recognition issue. Thus, you are *encouraged* to investigate accounting issues that are difficult and that we haven't covered, or won't cover, in class.
 - Companies with problems that have occurred within the past 5 years will be given more credit than problems that occurred longer ago.
- You will need to find financial statements for the company. Search for the company on the SEC Edgar system (which can be accessed through the Lippincott Library page) or check out the company's web site to ensure you have access to financial statements.
- If you have any questions, please feel free to talk to me about your choice of company to investigate.

Once you have chosen a company, write a report on the company that addresses the following issues:

1. Describe the economic transaction(s) underlying the questionable accounting. Discuss the transaction in the context of the company's business and strategy (you may need to look in the company's annual report for this material).
2. Describe the accounting procedure used by the company and the accounting procedure that "should" have been used according to the critics of the accounting practice. Journal entries may be helpful here in laying out the accounting. What is the basis or justification for the company's accounting practices and for the alternative accounting practices in terms of accounting rules and concepts? How detailed or forthcoming about the accounting procedure was the company in its annual report prior to the controversy?
3. What indications were there (if any) of the problem that an astute analyst might have seen in advance?

4. Do you agree with the critics that the company's accounting practices were wrong, given your answers to the above questions? Why or why not? Note that, just because a company gets criticized for its accounting, it is not necessarily doing the wrong thing. Microsoft has been investigated by the SEC numerous times for questionable accounting practices and has been cleared every time. Are there changes to accounting or auditing standards you would recommend based on what happened?
5. If the company were to restate its financial statements using the accounting procedure that "should" have been used, what would be the effect on the a) income statement, b) balance sheet, and c) statement of cash flows? You do not have to replicate the entire statement; you just need to indicate changes (e.g., accounts receivable would increase, net income would decrease, etc.)
6. Why do you think the alleged problem occurred?
7. What were the consequences of the revelation/resolution of the problem? What happened to the firm's stock price? Did anyone get prosecuted or sent to jail? Were any fines levied? Etc.
8. Does the revelation of the company's alleged flawed accounting practices change your assessment of the company's long-run value? If so, how? If not, why not? Here I want something more substantive than the statement "value is based on cash flow, not on accounting numbers."

Hand in the following:

- A written report which addresses these issues. There is no page or word limit on your write up of this assignment, but please use 12 pt. font and at least a 1" margin on each side.
- The article, analyst report, or SEC enforcement bulletin that alerted you to the situation.
- The most recent set of financial statements issued by the company prior to the controversy.
- Any other exhibits or material to support your analysis.

Exam

There will be a mid-term and final for this course.

Grading Disputes

All grading disputes must be appealed within *two calendar weeks* following the return of the assignment or exam (unless otherwise noted). *A request for a regrade will not be considered if it is submitted more than two week after the return of the assignment or exam (or after the specified deadline).* To have an assignment or exam regraded, you must submit the original (with no modifications) and a written description of your disagreement with the initial grade.

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Preliminary Course Outline

Session	Date	Topic	Case
1	Thurs, Jan 14 th	Course Introduction	
2	Tues, Jan 19 th	Setting for Financial Reporting	Enron
3	Thurs, Jan 21 st	Accrual Accounting – income Determination	Corbomax
4	Tues, Jan 26 th	Additional topics of Income Determination	C3-6 Clear One
5	Thurs, Jan 28 th	Structure of Balance Sheet and Cash Flows	Schering Plough
6	Tues, Feb 2nd	Essentials of Financial Statement Analysis	Whole Foods
7	Thurs, Feb 4 th	Role of Financial info in Valuation and Credit	Krispy Kreme Microsoft
8	Tues, Feb 9 th	CFO Perspectives	
9	Thurs, 11 th	Loan Agreements – Management Compensation	7-5 Computer Associates
10	Tues, Feb 16 th	Proxy Statements/Governance	Home Depot
11	Thurs, Feb 18 th	Receivables/Securitizations	Oakwood Homes
12	Tues, Feb 23 rd	Inventories	9-2 General Electric
13	Thurs, Feb 25 th	Long Lived Assets	TBA
14	Tues, March 2 nd	Current Issues in Financial Reporting	
15	Thurs, March 4 th	Midterm	

16	Tues, March 16 th	Financial Instruments	
17	Thurs, March 18 th	Present Cases	
18	Tues, March 23 rd	Present Cases	
19	Thurs, March 25 th	Reporting for Leases	Office Depot
20	Tues, March 30 th	Income Tax Reporting	13-2 Sara Lee
21	Thurs, April 1 st	Pensions and Post Retirement	14-1 14-2 General Motors
22	Tues, April 6 th	Equity and Earnings Per Share	Comcast
23	Thurs, April 8 th	Equity Investment and Variable Entities	Entities
24	Tues, April 13 th	Statement Formats	Nokia
25	Thurs, April 15 th	IFRS	
27	Tues, April 20 th	Conclusion and Wrap Up	
28	Thurs, April 22 nd	Open Time	
29	Tues, April 29 th	FINAL	