

Acct 743 (243)
Accounting for Mergers, Acquisitions, and Complex Financial Structures
Autumn Semester 2012

General Course Information

Aut disce aut discede (either learn or depart)

Instructor

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Registration

Acct 743 (243) serves as the Wharton School's advanced accounting class for both its graduate and undergraduate programs; being an "advanced" class, the material in this course is unavoidably difficult. Thus, students are *strongly discouraged* from registering for Acct 743 (243) unless they satisfy four criteria.

1. A student believes that he or she has achieved already a high level of proficiency in accounting, as demonstrated by having either received a top grade in his or her prior accounting preparation (e.g., nothing less than a grade of "A-" in any prior accounting class) or earned the equivalent of an accounting concentration in an accredited undergraduate business curriculum;
2. A student anticipates having sufficient time during the semester to handle a course with a heavy work load, which as a practical matter means that he or she has either already accepted a job offer or anticipates spending relatively little time in the recruiting process during the semester;
3. A student perceives that intellectually he or she is easily in the top 15% of his or her respective academic programs (e.g., Wharton MBA program; Wharton undergraduate program; Penn Law; etc.); and
4. A student is comfortable with material that is rigorous and quantitatively challenging, such as mathematics, engineering, computer science, etc.

For example, in the Autumn Semester of 2011 a total of *only* 49 (!) Acct 743 registrants successfully completed Acct 743. A student is discouraged from registering for Acct 743 (243) if he or she anticipates *any* problem with performing at a high level.

In addition, Acct 243 registrants are required to have *completed* successfully one of either Acct 201 or 202 *before* registering for Acct 243. Failure to have done so shall result in a student being dropped from the roster (the transcripts of all Acct 243 registrants shall be screened to ensure this policy is followed).

If a student has any doubt as to whether Acct 743 (243) is an appropriate class based on his or her personal circumstances, do not register!

"Blow-out" Sale

This is the last time we anticipate offering Acct 743 (243). While the reasons for not offering Acct 743 (243) in the future are complex, suffice it to say that over the last decade we have observed a steady decline in the willingness of MBA students to seek out coursework that is challenging and complex. As one MBA student opined recently, "I'd rather take a class that only requires that I sit in to listen to guest lecturers!" Nonetheless, as this is the last time we anticipate offering this class, as a (final) experiment I have reorganized the syllabus such that I intend to cover the most interesting material in the first $\frac{3}{4}$'s of the class: this material will be tested in 3 quizzes, with the last quiz scheduled for November 8. I intend to cover the most tedious and complex material in the last $\frac{1}{4}$ of the class: this material will be tested in 2

quizzes with the last quiz scheduled for December 6. Because this is the last time that we anticipate offering this class, as a “blow-out” sale I shall allow a student the following option:

1. Register for Acct 743 (243) under the auspices of “pass/fail”;
2. Take the first 3 quizzes;
3. Provided that a student shows “competency” in the first 3 quizzes, where competency is defined as maintaining an average not below two standard deviations of the pooled mean for *all* students who are registered for Acct 743 (243), he or she will receive a grade of “D” – a grade of “D” means that the student will pass the class.

A student who elects this option will not be subjected to quizzes or exams *after* November 8, and will avoid being tested on the most tedious material covered in this class. A student who does not elect this option, with the intent of achieving a grade higher than a “D,” *must take all 5 quizzes!*

Class Objectives

For all intent and purpose, this class is a traditional advanced accounting course, of the type commonly found at institutions with enough student interest to support an accounting major. For example, roughly 20% of the material tested on the CPA exam involves topics covered in an advanced accounting course. Key topics include the acquisition method for business combinations, the equity method for investments, the preparation and interpretation of consolidated financial statements, earnings-per-share considerations, the accounting implications of intercompany transactions, the accounting implications of non-domestic investments, etc. For a more detailed listing of individual topics, look below under “Topics” in the **Schedule of Assignments**.

This class pursues its objective in three ways. First, we analyze in detail the accounting that underlies each topic using the material found in any standard, advanced accounting textbook as a pedagogical guide for relevant issues. Second, through various lecture materials, cases, and exercises, we highlight and expand on these topics. Finally, we examine the financial statements of publicly traded companies to illustrate the application of these issues. The primary objective of the class is to become proficient in preparing and analyzing the financial statements of firms that merge and acquire other firms as part of their normal course of operations. Toward that goal, we attempt to understand the historical context and contemporary thought that has led to the promulgation of current accounting pronouncements on this topic.

This course is recommended to students who intend to work in the financial services area, broadly defined. Specifically, the course is recommended for students who, in their careers, anticipate that they will be required either to prepare pro forma consolidated statements for *prospective* acquisitions, or analyze the consolidated statements of *existing* complex financial structures.

Course Materials

A four volume set of course materials is available from **Study.Net**: Volumes I and II of lecture notes, Volume III of exercises, and Volume IV of suggested solutions to the exercises.

Supplementary Course Materials

Along with course materials of lecture notes and exercises, students are encouraged to have access to an advanced accounting textbook. Here I recommend two books.

Advanced Accounting, 11th Edition, Floyd A. Beams, Joseph H. Anthony, Bruce Bettinghaus, and Kenneth A. Smith (Pearson-Prentice Hall, NJ). This text is also on reserve in Lippincott Library.

Advanced Accounting, 2nd Edition, Susan S. Hamlen, Ronald J. Huefner, and James A. Largay III (Cambridge Business Publishers).

Academic Calendar

The University academic calendar shall be adhered to faithfully. Note that this academic year Fall Term Break on the University calendar is October 20-23. This means that there shall be no class on Tuesday, October 23.

Class Policies and Procedures

Classroom decorum

Zero-tolerance policy on class decorum. All classes start promptly. In addition, so as to cultivate the best pedagogical environment, food shall be prohibited from the classroom (students are permitted, however, to take one beverage to class). In addition, all text messaging, or other use of cell (mobile) phones, is strictly prohibited. *This policy shall be strictly enforced!* Students shall be directed to disable their phones *before* the start of each class.

Grading

Quizzes. Each quiz is closed-book, closed-notes, and individual product; “cheat-sheets” or other summaries of class material shall be strictly prohibited! Students shall be afforded the entire 80-minute class period to complete a quiz. Each quiz shall be graded based on 50 points. There is no final exam or quiz in the regularly scheduled final exam period.

Zero-tolerance policy on attendance at quizzes. Students are required to attend scheduled quizzes in the sections for which they are registered: *there are no “make-up” quizzes.*¹

Conflicts that result in missing a quiz shall be categorized as follows. A “Class A” conflict is something tantamount to a medical emergency. In the event of a medical emergency that incapacitates a student at the time of a scheduled quiz, and for which a student has documentation, that quiz shall be ignored and the student shall be graded exclusively based on his or her performance on the other four quizzes. In effect, a student’s cumulative performance on the other four quizzes shall be grossed up by 25%. A “Class B” conflict is something tantamount to an unforeseen conflict with another academic obligation. In the event that a student has a conflict of this nature, in place of the missing quiz the *lowest* score among the four other quizzes a student takes shall be substituted. A “Class C” conflict is anything deemed avoidable or frivolous. In this event a student shall be assigned a score of zero for that quiz.

I am the sole arbiter of the appropriate categorization of a conflict.

Grade distribution. Grade distribution shall be determined as follows. First, all Acct 743 registrants will be put in a single pool; the pool is subject to a fixed and immutable grade distribution whose mean cannot exceed 3.33. *The current electronic grading system employed by the MBA Office will not allow grades to be submitted electronically if they fail this criterion!* Second, all Acct 243 registrants shall be put in second pool; the grade distribution for the pool shall be determined based on performance relative to the Acct 743 pool (whose mean cannot exceed 3.33). Consider the following illustration. In a combined pool of 5 Acct 743 and Acct 243 registrants, the 1st, 2nd, and 4th best students by rank are Acct 743 registrants; the 3rd and 5th best students are Acct 243 students. I assign the 1st, 2nd, and 4th best students grades of A, B+, and B-: these grades average to 3.33. Thus, the 3rd best Acct 243 registrant must receive a grade no higher than B+ and no lower than B-; the 5th best Acct 243 registrant must receive a grade no higher than B- (and as low as I deem appropriate).

No class credit shall be given to any student whose performance on the five scheduled quizzes (or the first three scheduled quizzes if taking the class “pass/fail”) is more than two standard deviations below the

¹ Conflicts that arise from religious holidays on quiz dates shall be accommodated by providing a student with the opportunity to take a quiz the day *before* the regularly scheduled quiz date.

cumulative mean of all students in all sections of Acct 743 and 243 (i.e., the combined student pool).
There are no exceptions to this policy!

Re-grades. *Requests to re-grade quizzes are strongly discouraged!* If a student has a valid inquiry about how a quiz was graded, he or she should contact the grader by e-mail at **tblac@wharton.upenn.edu**, and then drop off his or her quiz with the grader by putting it in the mailbox of **T.Blackburne** in the Accounting Suite (1300 SH-DH). If it appears that a student is making persistent, and frivolous, re-grading requests, he or she shall be prohibited from making additional requests and this behavior shall factor into the student's CD&P-adjustment (see below).

Prior years' quizzes. Virtually every variation on every quiz from prior years has been converted into an exercise in this year's assignments. This accounts for the surfeit of exercises in the course materials.

This year's quizzes. Quiz answers and summary performance statistics shall be posted as soon as the grading has been completed.

Classroom decorum and participation (CD&P). A student shall be sanctioned for poor classroom decorum and participation in class (CD&P) through a reduction in his or her cumulative performance; this shall be referred to as a student's "CD&P-adjustment." A student's CD&P-adjustment shall be influenced by two factors. The first factor is class decorum, which is defined as class attendance and prompt arrival at class when a student attends. Students who arrive after class begins at the regularly scheduled class time, or fail to attend at all, shall be sanctioned through their CD&P-adjustment. The second factor is class participation. During class students are expected to participate in class discussions. Students who are unprepared to participate shall be sanctioned through their CD&P-adjustment. The default for the CD&P-adjustment is 0: that is, a student who attends class regularly and participates in class shall be subject to no adjustment to his or her cumulative performance on the five quizzes. Alternatively, students who exhibit poor class decorum and fail to participate shall be subject to an adjustment in a range between 0 and minus 50 points.

Cumulative point total. A student's cumulative point total shall be based on a student's cumulative performance in the five quizzes (which represents a total of 250 pts.), *less* the CD&P-adjustment (which ranges between 0 and minus 50 pts.).

Class credit. I reserve the right to deny class credit to any student whose performance I deem inadequate.

Assignments

Schedule of Assignments

The schedule of assignments begins on the next page. Note that I shall not test the material on three topics listed in the schedule of assignments:

1. "Tax Considerations in Mergers," scheduled for September 13;
2. "Corporate Liquidations & Reorganizations," scheduled for September 25.
3. "Preferred Stock, EPS, & Consolidated EPS," scheduled for October 16.

These topics are introduced simply to edify and provide perspective. A student is responsible for all other topics unless he or she elects the "pass/fail" option, in which case he or she is not responsible for topics after November 8.

Topics & Class Dates	Lectures, Readings, & Cases	Exercises
Overview	Overview	PSS #1 (Review of Financial Statement Preparation)
Class #1 Sept. 6	AmerisourceBergen (Merger Disclosure) AOL Time Warner (Goodwill Impairment) JDS Uniphase (Goodwill Impairment) Alcan (Merger Adjustments & Goodwill Disclosure)	Plastic & Synthetic (Merger) Pandemonium & Serenity (Computing Goodwill)
Balance Sheet Considerations in Mergers: An Historical Perspective Class #2 Sept. 11	Balance Sheet Considerations in Mergers: An Historical Perspective Intel (In-Process R&D) Yahoo! (Goodwill Allocations) USA Interactive (Intangible Assets vs. Goodwill)	Purloin & Steal (Business Combinations) Pumpkin & Squash (Business Combinations) Pistil & Stem (Business Combinations)
Tax Considerations in Mergers Class #3 Sept. 13	Tax Considerations in Mergers Spanish Step; European Telecoms, <i>The Economist</i> , 2005 Babcock and Wilcox (Taxable vs. Nontaxable Goodwill) United Retail Group, Inc. (Taxable vs. Nontaxable Goodwill)	PSS #2 (Tax Considerations)
Investments Class #4 Sept. 18	Investments General Motors (Investments)	Police & Siren (Consolidated Balance Sheet) Poem & Sonnet (Equity Investments) Port & Sauternes (Equity Method) PSS #3 & #4 (Financial Statement Preparation w/ Investments)

Topic & Class Dates	Lectures, Readings, & Cases	Exercises
<p>Consolidated Investments</p> <p>Class #5</p> <p>Sept. 20</p>	<p>Consolidated Investments</p> <p>A Once-Sweet Bottling Plan Turns Sour for Coke, New York Times, 1999</p> <p>Anheuser Busch, et al. (Subsidiary Investments)</p>	<p>Polka-Cola & Syrup (Consolidation)</p> <p>Politburo & Senate (Consolidation)</p> <p>Pepper & Salt (Bargain Purchase)</p> <p>Pilot & Stewardess (Bargain Purchase)</p> <p>Pasta & Salad (Equity Investments)</p> <p>PSS #5 & #6 (Consolidation w/ Multiple Investments)</p> <p>PSS #7 (Multiple Investments with Depreciable Asset Step-up)</p>
<p>Corporate Liquidations & Reorganizations</p> <p>Class #6</p> <p>Sept. 25</p>	<p><i>Fresh-Start Accounting: What Is the Implication on Reported Earnings of Companies Emerging from Chapter 11?</i>, Soo Kim (WG '06), 2006</p> <p>Enron Capitalism, etc.</p> <p>MFN Financial Corporation (Reorganization)</p> <p>MFN Financial Corporation's 1999 10-K & 2000 10-K (These will be posted on the class website in Wharton web café as the documents: MFN - 10K-1999.pdf and MFN - 10K-2000.pdf)</p>	
<p>Class #7</p> <p>Sept. 27</p>		<p>Quiz #1</p>
<p>Changes in Stock Ownership</p> <p>Class #8</p> <p>Oct. 2</p>	<p><i>Changes in Stock Ownership</i>, Katherine Daly (WG '09), 2009</p> <p>IMS Health Inc (SAB 51 Gains)</p> <p>Pharmacia & Monsanto (Consolidated Subsidiaries)</p> <p>Nextel Communications, Inc. (Deconsolidation Gains)</p>	<p>Pin & Stripe (SAB 51 Gains)</p> <p>Parasite & Sycophant (Changes in Ownership)</p>

Topic & Class Dates	Lectures, Readings, & Cases	Exercises
Working Paper Adjustments Class #9 Oct. 4	Working Paper Adjustments Lyondell Chemicals (Consolidation Issues), Josh Lewis (WG '06) Disney (Off Balance Sheet Investments)	Porcupine & Skunk (Working Paper Adjustments) Polygamous & Single (Working Paper Adjustments) Private-Eye & Sleuth (Working Paper Adjustments)
Intercompany Transactions – Inventories Class #10 Oct. 9	Intercompany Transactions - Inventory Stater Bros Holdings Inc (Unconsolidated Affiliate) Alcan & Novelis (Spin-off with unrealized, intercompany profits)	Push & Shove (Intercompany Inventory Transactions) Patio & Solarium (Intercompany Inventory Transactions) Portly & Stout (Intercompany Inventory Transactions) Python & Snake (Consolidation w/ Cost Data) Python & Snake Revisited (Consolidation w/ Cost Data) Petunia & Sunflower (Intercompany Inventory Transactions) Parsley & Sage (Intercompany Inventory Transactions) Port & Starboard (Consolidation w/ Cost Data)
Intercompany Transactions - Depreciable and Non-depreciable Assets Class #11 Oct. 11	Intercompany Transactions - Nondepreciable Assets Intercompany Transactions - Depreciable Assets	Prostrate & Supine (Intercompany Land Transactions) Prometheus & Sisyphus (Consolidations w/ Intercompany Transactions) Paranoid & Schizophrenic (Consolidations w/ Intercompany Transactions) Peregrine & Stork (Consolidation w/ Intercompany Transactions)
Preferred Stock, EPS, Consolidated EPS Class #12 Oct. 16	Preferred Stock, Earnings Per Share (EPS), and EPS Considerations in Business Combinations eBay (Expensing Employee Stock Options)	MLV (EPS) O'Lanahan Trick-n'-Prank Company (EPS) Principal & Student (Consolidated EPS) Porpoise & Squid (Consolidated EPS)
Class #13 Oct. 18	Quiz #2	

Topic & Class Dates	Lectures, Readings, & Cases	Exercises
Oct. 23 No Class!		Fall Break
Complex Affiliations Class #14 Oct. 25	Complex Affiliations	Parteehardee (Cross Holdings) Parteehardee Revisited (Cross Holdings w/ Goodwill Impairment) Pond, Stream, & Spring (Consolidation w/ Cross Holdings) Polygraph & Subsidiaries (Complex Affiliations)
Non-Domestic Investments Class #15 Oct. 30	Non-Domestic Investments Overview	
Foreign Currency Translations Class #16 Nov. 1	Foreign Currency Translations Amazon.com (Translating Intercompany Loans) Amazon (Translating Intercompany Loans), Peter Kim (WG '05)	Puccini & Strauss (Translation) Prague & Sarajevo (Translation) Paris & Seine (Translation) Providence Corporation (Translation) Peoria & Sofia (Translation)
Foreign Currency Remeasurements Class #17 Nov. 6	Foreign Currency Remeasurements	Postage & Stamp (Remeasurement) Philadelphia Corporation (Remeasurement) Prokofiev & Sibelius (Remeasurement)
Class #18 Nov. 8		Quiz #3

Topic & Class Dates	Lectures, Readings, & Cases	Exercises
Class #19 Nov. 13	Intercompany Transactions - Debt	Pusillanimous & Strong (Intercompany Debt) Prince & Squire (Intercompany Debt) Popeye & Sweatpea (Intercompany Debt) Plato & Socrates (Consolidations w/ Intercompany Transactions)
Class #20 Nov. 15	---	Putrid & Stinky (Interpreting Consolidated Statements) Pluto & Saturn (Interpreting Consolidated Statements)
Class #21 Nov. 20	Review Session to Prepare for Quiz #4	
Nov. 22 No Class!	Thanksgiving Break	
Class #22 Nov. 27	Quiz #4	
Capstone Cases Class #23 Nov. 29	The capstone cases cover the material in <i>Beams, et al.</i> , Chapters 5-7	Pencil & Sharpener (Consolidations w/ Data Flaws) Paparazzi & Sinema-Star (Consolidations w/ Data Flaws) Precipitous & Slow (Consolidation w/ Data Flaws) Pliable & Supple (Interpreting Consolidated Data)
Class #24 Dec. 4	Review Session to Prepare for Quiz #5	
Class #25 Dec. 6	Quiz #5	