

Accounting 742: Financial Reporting & Business Analysis

Course Overview

Financial data is employed in a multitude of analytical research and decision-making contexts such as equity valuation, bankruptcy prediction, acquisition decisions, and managerial performance assessments. In order for the data to be used effectively, however, the nature of the data itself must be understood. For example, effectively using a firm's quantitative history of reported sales revenue in forming forecasts of future cash flows requires an understanding of how the firm defines (i.e., measures) sales revenue. Accounting 742 is designed to increase your ability to understand and utilize the financial data provided in financial statements.

The primary focus will be on developing your ability to engage in accounting analysis, which is the process of assessing how the financial metrics reflect the underlying economic constructs of interest, as well as your ability to utilize or transform the financial data to gain insight into a firm's underlying business strategy, economic performance, and future outlook. For example, after taking this course, you should be able to use the disclosures in a firm's financial report to determine its accounting practices for a particular type of transaction and be able to determine how that policy choice affects its primary financial statements. Given your understanding of the drivers of the statements, you should be able to assess what, if anything, those statements communicate about the effectiveness of the firm's strategy, the firm's underlying economic performance, and the firm's future outlook. Furthermore, you should be able to recast the firm's financial statements to reflect accounting practices that you believe are intrinsically superior or that facilitate more meaningful comparisons with peer firms.

To meet the course objectives, we will rely extensively on case studies involving the financial disclosures of actual companies. Hence, this course is a case-based, as opposed to textbook-based course. Many of the cases are selected to illustrate that significant accounting analysis issues can arise from new organizational and technological innovations. For example, new derivative instruments, securitization vehicles, organizational forms, and intellectual property have all created challenging accounting issues.

The course is roughly divided into three topical areas: revenue recognition, expense recognition, and financial transactions. In the revenue recognition section we will consider questions such as: How do software providers record revenues for software contracts and how does that practice influence the analysis of revenues? How should a technology firm that bundles search and cloud services into a single contract record revenues for the various elements of that contract and how does that practice influence perceptions of value? How might a firm's innovative organizational structure interact with its value chain to distort perceptions of its revenue generating capacity? Why might a start-up firm emphasize non-GAAP measures of revenue instead of traditional GAAP measures of revenue recognition, and why might those measures be more useful for analysis purposes? In the expense recognition section, we will consider questions such as: How should a firm account for costs incurred to attract subscribers and how does that influence assessments of firm performance? How do firms in high R&D industries (e.g., biotechnology and pharmaceutical industries), alter their organization structures in response to R&D expense recognition rules? Why are multinational firms with a great deal of intellectual property (e.g., Apple) able to reduce their effective tax rates to levels substantially lower than statutory rates? Finally, in the financial transactions section, we will consider questions such as: How are derivative contracts reflected in financial statements, and it is possible to distinguish hedging from speculative activities? How do intangibles acquired (e.g., in process R&D, goodwill, and unexecuted contracts) via mergers and acquisitions activity affect future performance metrics?

Note: If you found your introductory accounting course extremely challenging and/or stressful, you might consider taking ACCT 742 as a pass/fail course. If you do, keep in mind that Pass grades are not eligible for LT designations but Fail grades will result in an LT.

Preparation and Performance, Quizzes, Exam, and Project

Class Preparation and Participation

Prior to almost all classes, you will be expected to read through a case, perhaps watch a video, and complete some class preparation questions. The goal of the class preparation questions is simple – to induce you to read and think about the material to be discussed in class. Note that the class discussion will build off of the class preparation questions. To obtain credit, you must complete the preparation materials when they are due. No exceptions.

In most instances, the case studies will rely heavily on verbatim excerpts from the actual financial filings (e.g., 10-K reports and 8-K press releases). For those of you who are more comfortable dealing with textbook like problems or highly polished and sanitized cases, dealing with the source material directly will prove frustrating and maddening at times. Unfortunately, that is the way it is when you leave the cloistered halls of academe. By actively engaging in the learning-by-dong (or, in some instances, learning-by-suffering) exercises provided by the cases, however, you will become more comfortable working with real financial statement data.

Quizzes

There will be two quizzes during the semester. The quizzes will be somewhat cumulative in the sense that you are responsible for all topic areas covered up to and including that quiz, although each quiz will be heavily skewed towards the topics covered since the prior quiz. To assist you in preparing for the quizzes, there will be practice posted on Canvas.

Final Exam

The final exam will be a cumulative exam based upon a single set of financial statements. You can use any written reference resources including your notes, GAAP guides, textbooks, etc. during the exam. To assist you in preparing for the final exam, there will be a practice exam posted on Canvas. Note that completing the practice exam is not nearly sufficient for preparing for the exam. You should review the material covered during the classes, the quizzes, and the practice problems as well.

Project

You will prepare an Accounting Analysis project with a group of 2 to 4 fellow students (each group can have no less than 2 and no more than 4 students – no exceptions). You have two project options. Under Option 1, your group to complete a thorough analysis of the financial statements of a company selected by you. Your group, however, should select a company with at least one interesting/contentious accounting issue that has significant consequences for the “look and feel” of the financial statements. Your second option is to identify a current accounting issue being or recently considered by FASB/IASB and to evaluate the issue(s), approaches for resolving those issue(s), and to critique or defend FASB’s/IASB’s resolution to the issue (if applicable). More information regarding the project assignment is available on Canvas.

Grading

Grades will be based upon the following allocation scheme:

| | |
|-----------------------------------|-----|
| Class Preparation and Performance | 15% |
| Quizzes | 30% |
| Final Exam | 30% |
| Project | 25% |

To pass the course you must pass the final exam.

Class Materials

Canvas

Class Preparation Materials

In advance of each class you should work through the material required for the pre class quiz associated with that class. The quiz can be found in the assignments tab of the Canvas site. The files associated with each class can be found in the files tab, and there will be a folder for each class. Within each folder will be three subfolders. The subfolder labeled Pre Class Materials will include cases, problems, or teaching notes that should be read prior to class. These items can be linked from the quiz page as well. The subfolder labeled In Class Materials will contain class slides as well as any other material we will cover in class that is not included in the Pre Class Materials. The class slides will be available at 6:00 PM the evening before class. The Post Class Material Subfolder contains material distributed during class, brief technical notes for the cases or problems discussed, and optional readings related to what was covered in class. This material will be made available at the end of the day that the class session is held.

Your Introductory Text or a GAAP Guide

There is no text for the class. Your introductory text can provide a useful reference for some of the material we will cover. You also might find a GAAP guide useful for reference purposes. More than one publisher offers a GAAP Guide (e.g., CCH and Wiley). In general, a GAAP Guide provides a good overview of technical accounting by topic area as well as references to the Accounting Standards Codification (ASC). Note that most students, however, will survive just fine on the class materials and the occasional web search.

FASB Accounting Standards Codification (ASC)

You will also have access to the Financial Accounting Standards Board's (FASB's) searchable accounting standards codification (ASC). The ASC is a great reference for technical accounting, although it is not necessarily the user-friendly. (It becomes friendlier with use.) To access the FASB site go to

<http://www2.aaahq.org/ascLogin.cfm>

The username is AAA51620 and the password is KR4K4Dx. Please logoff when you are done.

Instructor Availability

You can reach me at my email address, which is pef@upenn.edu. Virtual office hours are by appointment. If you reach out to me and want to meet ASAP, I will endeavor to accommodate you. If I cannot meet immediately, I will try to arrange to speak with you sometime that same day. Virtual office hours will generally be conducted on Zoom unless you request otherwise.

Accounting 742: Accounting and Business Analysis
Spring 2021
Summary Class Schedule (Tentative)

| Session | Day | Date | Topics | Case(s) |
|---------|----------|-------|---|------------------------|
| 1 | Thursday | 01/21 | Introduction | |
| 2 | Tuesday | 01/26 | An Innovation Principal Financial Statements: Statement of Cash Flows | TACTEC |
| 3 | Thursday | 01/28 | Understanding Financial Reporting for Taxes | MDC |
| 4 | Tuesday | 02/02 | Tax Planning Innovations: The Case of Intellectual Property | Ebix II |
| 5 | Thursday | 02/04 | Revenue Recognition Fundamentals | MiniCases |
| 6 | Tuesday | 02/09 | Revenue Timing: Online Marketplace | eHealth |
| 7 | Thursday | 02/11 | Reporting Innovations and Comparability: Accounting Policy Changes | Homex |
| 8 | Tuesday | 02/16 | Sales or Subscriptions: Revenue Recognition for Software Services | IT Associates |
| 9 | Thursday | 02/18 | Organizational Innovation and Revenue Generation | Mediterranean Express |
| 10 | Tuesday | 02/23 | Innovating Beyond GAAP: Non GAAP Reporting Metrics | Tesla |
| 11 | Thursday | 02/25 | Driving Sales With Consumer Financing | Cavco |
| 12 | Tuesday | 03/02 | TBA | TBA |
| 13 | Thursday | 03/04 | Expense Recognition Fundamentals | |
| 14 | Tuesday | 03/09 | Quiz 1 (Session 1 to Session 12) | |
| | | 03/11 | Spring Break | |
| 15 | Tuesday | 03/16 | Customer Acquisition Costs | Prepaid Legal |
| 16 | Thursday | 03/18 | Program Accounting (Hopes and Dreams?) | Boeing |
| 17 | Tuesday | 03/23 | Organizational Innovation: Coping with R&D Expensing | Alza |
| 18 | Thursday | 03/25 | Organization Boundaries | Grand Canyon Education |
| 19 | Tuesday | 03/30 | Contingent Compensation/Earnings Per Share | |
| 20 | Thursday | 04/01 | Contracts, Commitments, and Contingencies/Leases | Par Pharma |
| 21 | Tuesday | 04/06 | Long-Term Debt and Fair Value Accounting | MGM |
| 22 | Thursday | 04/08 | Breaking Old Promises: Pensions and Other Post-Employment Benefits | Musselman Steel |
| 23 | Tuesday | 04/13 | Financial Innovations: Derivatives and Hedging | Southwest Airlines |
| 24 | Thursday | 04/15 | Organizational Boundaries: Control and Significant Influence | Coca-Cola |
| 25 | Tuesday | 04/20 | Quiz 2 (Session 13 to Session 23) | |
| 26 | Thursday | 04/22 | Acquired Intangibles | Shaw Group |
| 27 | Tuesday | 04/27 | Consolidating Foreign Entities | |
| 28 | Thursday | 04/29 | Summary and Conclusion | |
| | | | Final Exam: 6:00 PM to 9:00 PM (Tentative) | |