

FINANCIAL ACCOUNTING
Winter Term 2012

Professor Robert J. Resutek
Tuck 202; 6-9635
Office hrs: Friday 3-5pm

Course Objectives

The role of accounting is to provide information to investors, policy-makers, regulators, and other decision-makers to facilitate the allocation of resources in society. The purpose of this course is to understand the accounting process and to develop skills necessary to evaluate an enterprise's financial position and its operating, investing and financing activities.

The course gives students the necessary background to: (1) understand the concepts and *measurements* that underlie financial statements, (2) develop the skills needed to *analyze* financial statements effectively, and (3) gain an understanding of the choices enterprises make in *reporting* the results of their business activities. The first part of the course emphasizes the measurement concepts and the mechanics of moving from business transactions to the principal financial statements: balance sheet, income statement, and statement of cash flows. The second part introduces tools for analyzing financial statements, with an emphasis on integrating industry economic and business strategic factors into the analysis and interpretations. The third part focuses on generally accepted accounting practices (GAAP) for particular topics, such as the timing of revenue recognition, inventory valuation, and measuring the amount and cost of debt financing, with an emphasis on how management's choices among alternative GAAP affect the quality of earnings and reported financial position.

The course emphasizes interactive case discussions based on analysis of actual companies' financial statements. Accordingly, the course provides an opportunity to develop skills necessary to critically evaluate firms' actions and the efficiency with which they have managed their resources.

Course Materials

- Textbook: *Financial Accounting: An Introduction to Concepts, Methods, and Uses*, by Stickney, Weil, Francis & Schipper, 13th edition.
- Course packets (CP) of cases and other materials at Wheelock Books. Estimated cost of the course packets is \$30.
- Additional materials will be posted to Blackboard.

Class Preparation and Participation

Class preparation consists of (1) text readings, (2) assigned problems, and/or (3) cases from the text or course packet. You should be prepared to present your analysis of all aspects of an assignment in class. Optional problems are suggested if you find that you need either guidance before preparing the assigned problems and cases or additional practice to reinforce the concepts covered in class. Solutions to the optional problems are in the course packet or accessible via your personal online account.

The most important requirements for this course are thorough preparation and analysis of the assigned problems, cases and reading materials, and active participation in class. To excel in this class, a student needs to set aside time to study the material on consistent basis. Students who procrastinate studying and try to learn the material immediately before an exam or an expected quiz will not perform well.

You are asked to turn in solutions to assigned problems and/or cases for most classes. These assignments are meant to be a learning tool and a way to gauge your level of understanding. You are encouraged to work through homework problems and to prepare for cases in groups. However, each student is *individually* responsible for turning in each assignment and for answering case-related questions in class.

Your class participation grade is affected by general classroom behavior. You will lose points in this category for: being absent without informing your professor ahead of time, not bringing name cards to class, coming late to class or leaving class early, or exhibiting behavior considered obstructive to the learning of other students in class (such as leaving and returning to class while it is in session, surfing the web and checking e-mail, and voicing inappropriate comments).

Grading

The course grade will be based on a mid-term examination, a final examination, submitted assignments, quizzes, and class participation. The midterm will emphasize material covered in sessions 1 to 9. The final examination will emphasize material covered in sessions 10 to 19. There is, however, a cumulative nature to the material in this course, so that some testing of earlier material is inevitable. There will be four short quizzes (10 minutes) given during the term. Students can drop their lowest quiz score. Missed quizzes count as a drop. Examinations and quizzes will be closed book and notes. Hand-held calculators may be used for mathematical calculations only.

The following guidelines will be used to evaluate your overall performance:

Mid-term Exam	30%
Final Exam	40%
Quizzes	10%
Class Participation	10%
Homework	10%

Students who perform poorly on the midterm examination will have the option of taking an alternative final exam. The alternative final exam will focus on the core concepts of financial accounting, concepts that are primarily covered in the first 4 weeks of the course. The maximum course grade for students who choose this option will be a C+.

The alternative final examination option is targeted to students who find themselves behind in the material after the first half of the course and are concerned about failing the course. Any student who is in danger of failing the course will be confidentially notified after the midterm examination and offered this alternative examination option. Students choosing this option will still be responsible for the weekly homeworks and for the material covered on the quizzes. However, their final examination will not cover the more advanced material. Any student who wishes to take the alternative final exam has this option. That is, the option is not just available to students who perform poorly on the midterm; rather, any student has the option.

I do not anticipate that I will need to fail any student. However, students who fail to exert any effort in the class and/or students who cannot demonstrate even a reasonable level of proficiency with basic financial accounting concepts after 10 weeks will be in danger of receiving a failing grade. I will discuss this area thoroughly in the first day of class. Students should not hesitate to contact me with any additional questions regarding the computation of the grades.

Students with disabilities enrolled in this course that may need disability-related accommodations are encouraged to make an appointment to see me before the end of the second week of the term. All discussions will remain confidential, although the Student Disability Services office may be consulted to discuss appropriate implementation of any accommodation requested.

Course Representatives

By the end of the second week of class (1/13), I expect each section to have nominated 1-2 seniors to serve as the section's course representative. The purpose of the course representative is to serve as a way for students to submit anonymous feedback to me in a real time manner. Students are encouraged to submit to the course representative general concerns/suggestions about the class. The course representative's responsibility is to aggregate this information and pass it on to me when he/she feels it is warranted. In other words, the course representative's responsibility is to filter the substantive comments/suggestions from the trivial ones. Course representatives will meet with me at least 1-2 times a semester (or when warranted) to discuss any issues raised by students. Feedback from these meetings will be discussed in class.

Honor Code

This course will be conducted in strict conformity with the Academic Honor Code. The Code and related procedures can be found at

<http://www.dartmouth.edu/~reg/regulations/undergrad/acad-honor.html>

The site also contains comprehensive information on how to be sure that you have not plagiarized the work of others. Claimed ignorance of the Code and related information appearing on the site will be viewed as irrelevant should a violation take place.

Homework Policy

When noted in the syllabus, students are expected to turn in a hardcopies of their homework. Homeworks that require a hard copy to be submitted are case-based homeworks. Students are encouraged to begin work on the homework assignments prior to the respective lecture covering the material. There is no late policy for homeworks. Electronic submission of the case write-ups is reserved for students with an illness that prevents them from submitting their homeworks in hardcopy form or for students who are not on campus (e.g., travelling to a varsity sport or club-sponsored event). Please note, if you fall into one of these two categories you need prior permission to submit homework electronically.

Homeworks are graded on a '0', '1', '2' basis. I expect that most students who exert any effort on their homework to receive full credit.

Absenteeism due to Illness

If you are too ill to attend class, you must email me prior to class. Students absent from class due to illness (or any other reason) are still responsible for the respective homework assignments. These assignments can be submitted electronically via email. Missed quizzes cannot be made up and will count as the student's dropped quiz. Absenteeism due to illness should be an infrequent occurrence. Students who must miss multiple classes due to an extended illness should contact me (preferably via email or phone) and let me know of the details of their illness and I will try to accommodate the student as best as possible.

Electronic Homework Submission

Students submitting case assignments electronically must format their homework to print properly with *no additional formatting required by the grader*. The student's name, section, and the individual case must appear on the top of *each* individual homework assignment (i.e., if two homeworks are due, two separate homeworks need to be submitted). Students who do not format their homeworks to print properly will automatically receive half credit (at most).

Learning Objectives and Assignments

Notations defined:

- * denotes homework assignment to be handed-in.
- CP denotes cases / reading materials in the **C**ourse **P**acket.
- CASE denotes cases subject to cold calls during class.

I. Financial Measurement

Week 1 (1/3, 1/5)

Sessions 1&2: Overview of Business Activities and Principal Financial Statements

Learning Objectives:

1. Discuss the relation between accounting and economics and the role of accounting information in the functioning of capital markets.
2. Obtain an overview of the principal activities of business firms and how they relate to the three principal financial statements.
3. Observe the types of information provided by the three principal financial statements and how firms might use this information in managing and evaluating a business.

Assignment: Read Chapters 1&2.

Prepare: WhoAmI Case (CP)

Week 2 (1/10, 1/12)**Session 3: The Balance Sheet: Measuring Financial Position**

Learning Objectives:

1. Understand that the purpose of the balance sheet is to report the results of a firm's investing and financing activities at a moment in time.
2. Apply the accounting concepts for asset and liability recognition and valuation under generally accepted accounting principles (GAAP).
3. Discuss the historical development of the double entry recording framework with particular emphasis on how modern accounting practices developed from mercantile trade in Europe in the 1400s.
4. Apply the dual-entry recording framework to a series of transactions that results in a balance sheet.

Assignment: Read Chapter 3.

Prepare: Small Beginnings Corporation (CP)*.

Session 4: The Income Statement: Measuring the Results of Operating Performance

Learning Objectives:

1. Understand differences between the cash basis and the accrual basis of income recognition.
2. Understand and apply the accounting concepts for revenue and expense recognition and measurement under the accrual basis.

Assignment: Read Chapter 4.

Prepare: Mary Lou's Educational Services (CP)*.

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Week 2 Homework due 4pm on 1/13:

Small Beginnings Corporation (CP)*, Mary Lou's Educational Services (CP)*.

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Week 3 (1/17, 1/19)

Session 5: The Income Statement (continued)

Learning Objectives:

1. Apply the dual-entry recording framework to a series of transactions that results in a balance sheet and an income statement.
2. Discuss the corporate governance issues at WorldCom. Also discuss how WorldCom, Enron, Adelphia, HealthSouth, and others, motivated key provision of the Sarbanes-Oxley Act.

Prepare: WorldCom CASE (CP)*.

Session 6: The Statement of Cash Flows: Measuring the Cash-Flow Effects of Operating, Investing, and Financing Activities

Learning Objectives:

1. Understand the rationale for, and the information value of, the statement of cash flows.
2. Develop skills in transforming income statement data to cash flow data and vice versa.

Read: Chapter 5.

Prepare: Seasoned Company (CP)*, Tertia (CP)*.

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Week 3 Homework due 4pm on 1/20

WorldCom (CP)*, Seasoned Company (CP)*, Tertia (CP)*

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Week 4 (1/24, 1/26)**Session 7: The Statement of Cash Flows (continued)**

Learning Objectives:

1. Reinforce skills in transforming income statement data to cash flow data and vice versa.
2. Consider relations between net income and cash flow from operations and between cash flows from operating, investing, and financing activities for various types of businesses.

Prepare: Aston Corporation (CP)*

II. Financial Analysis**Session 8: Introduction to Financial Statement Analysis**

Learning Objectives:

1. Introduce tools for analyzing a firm's overall profitability (rate of return on assets) and examine how profit margin and asset turnover ratios provide information about the economics and strategy of a business.
2. Introduce the Du Pont formula - a tool for analyzing a firm's return to shareholders.
3. Understand the effect of financial leverage on a firm's ROE.
4. Introduce tools for analyzing a firm's short-term liquidity risk (including its working capital management) and its long-term solvency risk.

Assignment: Read Chapter 6.

Prepare: Wal-Mart CASE (to be posted to Blackboard)

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Week 4 Homework due 4pm on 1/27:

Aston Corp. (CP)*, Wal-Mart Profitability and Risk CASE (CP)*

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Week 5 (1/31, 2/2)**Session 9: Pro Forma Financial Statements**

Learning Objectives:

1. Reinforce the relations between the three principal financial statements by preparing pro forma financial statements from a given set of assumptions.
2. Assess sensitivity of the financial statements to variations in pro forma assumptions.
3. Discuss which assumptions drive the various ratios in the Du Pont formula.

Prepare: Wal-Mart ProForma Case (to be posted to Blackboard)

III. Financial Reporting**Session 10: Quality of Earnings, Accounts Receivable and Revenue Recognition**

Learning Objectives:

1. Develop an understanding of the concepts of quality of earnings and identify incentives faced by a firm's managers in choosing methods of measuring and reporting business activities.
2. Discuss the recognition of revenue for firms in different industries.
3. Identify matching issues confronted in recognizing income at the time of sale of goods and services.
4. Understand the allowance method for uncollectible accounts.

Read: Chapter 7.

Prepare: Apple CASE (CP)*

Week 5 Homework due 2pm on 2/7:Apple CASE (CP)*

Midterm Exam 2/3*time and place to be announced*Exam will test material from sessions 1 through 9

Week 6 (2/7, 2/9)

Session 11: Inventories and Cost of Goods Sold

Learning Objectives:

1. Apply the principles of accrual accounting to manufacturing firms, distinguishing between product costs and period expenses.
2. Calculate inventories and cost of goods sold under FIFO and LIFO cost flow assumptions.
3. Understand how differences in inflation rates, growth rates, inventory turnover rates and other factors cause inventories and cost of goods sold to differ under FIFO and LIFO.
4. Discuss the LIFO Conformity rule as an outcome of a political process.

Read: Chapter 8.

Prepare: General Electric CASE (CP)*.

Optional Problems: 8-23, 8-26, 8-29, 8-46.

Session 12: Non-current Assets and depreciation and amortization expense

Learning Objectives:

1. Observe the difficulties applying GAAP to property, plant and equipment and to intangible assets and the effects on assessments of the quality of earnings.
2. Observe the effects of a firm's capitalization policy on balance sheet and income statement amounts.
3. Discuss goodwill measurement as an outcome of a political process.

Read: Chapter 9.

Prepare: Southwest Airlines CASE (CP)*

Optional Problem: 9-14, 9-21, 9-28, 9-32

Week 6 Homework due 4pm on 2/10:

General Electric CASE (CP)*; Southwest Airlines CASE (CP)*

Week 8 (2/14, 2/16)**Session 13: Liabilities/Bonds and interest expense**

Learning Objectives:

1. Understand the impact of the recognition and valuation of liabilities on assessments of profitability and risk.
2. Calculate the issue price and subsequent market value of bonds with various cash flow patterns using present value techniques.
3. Apply GAAP for long-term bonds at the date of issue, during each subsequent period prior to maturity, and at maturity.
4. Understand the reasons why the book value of bonds under GAAP at any date may differ from the market value of the bonds.

Read: Chapter 10 (p. 461-477) and Appendix *Time Value of Cash Flows* in textbook

Prepare: 10-30*, Sysco Corporation CASE (CP)*.

Optional Problems: 10-16, 10-18, 10-19, 10-29

Session 14: Accounting for Leases

Learning Objectives:

1. Understand the issues involved in structuring leases as operating leases versus capital leases and the financial statement effects of each accounting method.
2. Apply the operating and capital lease methods.

Read: Chapter 9 (see section titled *Leases*, p. 482).

Prepare: Adair Corporation (CP)*

Optional Problems: 10-28, 10-35.

Week 8 Homework due 4pm on 2/17:

10-30*; Sysco Corporation CASE (CP)*; Adair Corporation (CP)*.

Week 9 2/21, 2/23)

Session 15: Leases (continued) and Shareholders' Equity

Learning Objectives:

1. Capitalization of operating Leases
2. Understand the most common components of shareholders' equity.
3. Understand the economics events that alter stockholders' (or owners') equity, and how to account for them.

Read: Chapter 14.

Prepare: Target Corporation CASE (CP)*.

Optional Problems: 14-26, 14-31.

Session 16: Shareholders' Equity (continued) and Accounting for Employee Stock Options

Learning Objectives:

1. Understand the most common components of shareholders' equity.
2. Understand the economics events that alter stockholders' (or owners') equity, and how to account for them.
3. Understand the various elements that affect the value of a stock option.
4. Evaluate GAAP accounting for stock options and discuss the accounting for stock options as an outcome of a political process.
5. Analyze the impact of stock options on reported earnings.

Read: Chapter 14.

Prepare: 14-17*

Optional Problem: 14-23, 14-24, 14-28, 14-34

Week 9 Homework due 5pm on 2/24:

Target Corporation CASE (CP)*; Problem 14-17*

Week 9 (2/28, 3/1)

Session 17: Basics in Equity Valuation

Learning Objectives:

1. Explore the similarities/differences between various valuation models.
2. Understand the assumptions that drive the models differences.
3. Understand the accounting adjustments to reconcile valuation models

Read: Valuation notes, to be posted to Blackboard

Prepare: TBD.

Session 18: Advanced Financial Statement Analysis – Pulling it all together

Learning Objectives:

1. Incorporate adjustments for manager discretion into financial statement ratios.
2. Determine which financial ratios are critical to a given firm and/or industry.
3. Understand where the key assumptions to any set of financial forecasts lie.
4. Discuss forecasting horizon and terminal value assumptions.
5. Compare and contrast different ‘plug’ options within a set of financial statement forecasts.

Read: FSA notes, to be posted to Blackboard

Prepare: TBD.

Week 10 (3/6)

Session 19: Course review

Review material covered in the course

Final Examination

To be announced at a later date
