Course Objectives
This course is designed to prepare you to interpret and analyze financial statements effectively. This course explores in greater depth financial reporting topics introduced in the core course in financial accounting and also examines additional topics not covered in that course. The viewpoint is that of the user of financial statements. However, we develop sufficient understanding of the concepts and recording procedures to enable you to interpret various disclosures in an informed manner. We discuss each financial reporting issue in terms of its effect on assessments of a firm’s profitability and risk. We then apply the analytical tools and concepts in competitor analysis, credit decision, bankruptcy prediction, and valuation. This course is designed primarily for students who expect to be intensive users of financial statements as part of their professional responsibilities.

Course Materials
The readings, problems and cases for the course come from Financial Reporting and Statement Analysis: A Strategic Perspective, 5th edition, by Clyde Stickney, Paul R. Brown and James Wahlen (FRSA). I will also be posting reading materials periodically on Blackboard for class discussions.

Three internet addresses may prove useful to you at some point in the course:


Assignments
Readings, cases and/or problems are assigned for each class. You should come to class prepared to discuss your analysis of the cases and problems. Regular class participation is important to the learning process for you and your classmates. If collected, assignments are due at the end of the class assigned. No late assignments are accepted, nor are faxes or e-mailed assignments.

All assignments should be prepared using word processing software with type size no smaller than 12 point. During class discussions, please feel free to make any changes to
Your solutions, but do so in a way that clearly indicates that they are the result of class discussions (e.g., using a different color of ink).

You may work in groups to discuss homework assignments. However, each person should prepare his/her own individual homework solutions to be submitted. Ideally you should work through each day’s assignment on your own before discussing it with anyone. You can make changes to your solution based on your learning in any discussions. Interpretations of the analysis should be in your own words.

**Examinations**

There will be two exams given in the course. Both exams will be open book and notes. No make-up exams are given if you miss the first exam. The weight attached to the first exam will be assigned to the Final exam. You MUST sit for the Final exam. The exams will be given in class and are open book and notes.

**Group Assignment**

A separate hand-out will be distributed in the first class providing the details of the group assignment.

**Grading**

Grades will be based on the following weights:

<table>
<thead>
<tr>
<th>Component</th>
<th>Weight</th>
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<tbody>
<tr>
<td>Exam 1</td>
<td>35%</td>
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<tr>
<td>Final Exam</td>
<td>40%</td>
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<tr>
<td>Class Participation</td>
<td>5%</td>
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<tr>
<td>Group Assignment</td>
<td>20%</td>
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Topics and Assignments

Class 1 – February 11

Topics:  Introduction to Course and Financial Statement Analysis
         Initial Review of Zale Corporation Consolidated Financial Statements

Learning Objectives:

1. Overview of financial reporting and financial statement analysis.
2. Understand most effective means of mastering course and financial statement analysis.
3. Review the purpose, underlying concepts, and accounting principles related to the balance sheet, the income statement, and the statement of cash flows.

Read: *FRSA*, Chapter 1
Review: Zale Corporation Financial Statements
Prepare: Problem 1.1

Class 2 – February 18

Topics:  Financial Reporting Highlights and Introduction to Statement of Cash Flows

Learning Objectives:

1. Review key principles that drive the preparation of financial reports.
2. Understand the environment in which financial reporting principles are determined, as well as the limitations presented when analyzing a firm using financial reports.

Read: *FRSA*, Chapters 1 and 3
Prepare: *FRSA*, Case 1.1 and Problem 3.2

Class 3 – February 25

Topics:  Statement of Cash Flows

Learning Objectives:

1. Understand the relation between net income and cash flow from operations for firms in various industries.
2. Understand the relation between cash flows from operating, investing, and financing activities for firms in various stages of their life cycles.
3. Prepare a statement of cash flows from balance sheet and income statement data.

Read: *FRSA*, Chapter 3

Prepare: Problem 3.4, Problem 3.6, Problem 3.9

Class 4 – March 4

Topics: Profitability and Risk Analysis

Learning Objectives:

1. Master the ability for deciding when and how to adjust reported income in order to use it in evaluating performance and predicting future earnings of a firm.
2. Analyze and interpret changes in the operating profitability of a firm using the rate of return on assets and its components, profit margin and total assets turnover.
3. Analyze and interpret changes in the rate of return on common shareholders’ equity including condition when a firm uses financial leverage successfully.
4. Understand the benefits and risks of financial leverage and apply analytical tools for assessing short-term liquidity risk.
5. Understand the benefits and risks of financial leverage and apply analytical tools for assessing long-term solvency.
6. Understand how financial statements can be used to predict bankruptcy probabilities.

Read: *FRSA*, Chapters 4-5

Prepare: Case 4.1, Case 4.2, Case 5.6
Class 5 – March 11

Topics: Profitability and Risk Analysis (continued) with Quality of Accounting Information and Adjustments to Reported Financial data

Asset and Liability Valuation and Income Measurement

Deferred Income Taxes

Learning Objectives:

1. Develop an understanding of the concept of “earnings quality” with emphasis on the sustainability, measurement and manageability of reported earnings.
2. Discuss the link between the valuation of assets and liabilities on the balance sheet and the measurement of income.
3. Understand the need for recognizing deferred income tax expense when book income differs from taxable income because of temporary differences.
4. Understand the conditions that give rise to deferred tax assets and deferred tax liabilities.
5. Use disclosures of individual deferred tax assets and deferred tax liabilities to study amounts recognized for financial and tax reporting.
6. Use disclosures of the effective tax rate to understand why a firm’s average tax rate differs from the statutory tax rate.

Read: FRSA, Chapters 2 and 6

Prepare: Problem 2.5, Problem 2.9, and Problem 6.1

Class 6 – March 25

Topics: Income Recognition, LIFO Footnote adjustments, Fixed Assets, Intangibles

Learning Objectives:

1. Observe the effects of the financial statements of recognizing income prior to the time of sale, at the time of sale, and subsequent to the time of sale.
2. Observe the time series pattern of income when firms recognize income prior to the time of sale, at the time of sale, and subsequent to the time of sale.
3. Review the accounting for inventories and depreciable assets.
4. Examine the impact on assets and net income of capitalizing and amortizing intangibles development.
5. Identify the financial statement effects of alternative ways of organizing research and development activities and restate the income statement to a format that enhances analysis of the profitability of a technology-based firm.

Read: *FRSA*, Chapter 7

Prepare: Problem 7.1, Problem 7.2, Problem 7.5, Problem 7.6

Class 7 – April 1

Topics: Exam 1

Class 8 – April 8

Topics: Liability Recognition and Valuation

Learning Objectives:

1. Understand the concept of accounting liability to various transactions intended to keep debt off the balance sheet.
2. Observe the importance of identifying the entity bearing the risks and enjoying the economic return when deciding liability recognition issues.

Read: *FRSA*, Chapter 8

Prepare: Problem 8.1, Problem 8.4, Problem 8.6

Class 9 – April 15

Topics: Pension and Healthcare Benefits

Learning Objectives:

1. Distinguish between the amounts that firms report on their financial statements with respect to a pension or healthcare benefit plan and to the amounts that appear on the financial statements of the pension or healthcare benefits fund and understand why the two differ.
2. Use pension and healthcare disclosures to measure the economic status and financial performance of a pension or a healthcare benefits plan.
3. Observe the role of actuarial assumptions in accounting for pensions and healthcare benefits.
4. Understanding reserves in the financial statements.
Class 10 – April 22

Topics: Intercorporate Entities

Learning Objectives:

1. Understand the purchase method for accounting for a corporate acquisition, and its on-going effects on the financial statements.
2. Observe the interaction between legal, accounting, tax, and financing factors in structuring a corporate acquisition.
3. Understand the general principles for translating financial statements of foreign subsidiaries.

Read: FRSA, Chapter 9

Prepare: Problem 9.1, Problem 9.2

Class 11 – April 29

Topics: Forecasting Pro Forma Financial Statements

Learning Objective:

1. Review the relations between items on the balance sheet, income statement, and statement of cash flows that require consistency when preparing pro forma financial statements.
2. Design pro forma statements as support for adding a new product line, starting a new business, divesting of current businesses, etc.

Read: FRSA, Chapter 10

Prepare: Problem 10.6

Class 12 – May 6

Topics: Final Exam