

# Index

## *Numerics*

8-K form, 13, 251–253  
10-K form, 12, 247–250  
10-Q form, 12, 246–247  
1065 form, 20

## • A •

AAERs (Accounting and Auditing Enforcement Releases), 314  
account format, balance sheet, 76  
accounting  
  accrual, 42, 43–44, 333  
  cash-basis, 42, 43–44, 334  
  Chart of Accounts, 48–55  
  debits and credits, 44–48  
  double-entry, 8, 45, 335  
  overview, 41  
  profit, 55–56  
  when company's in trouble, 330  
Accounting and Auditing Enforcement Releases (AAERs), 314  
accounting policies note  
  changes in, 134–135  
  depreciation, 121–122  
  expenses, 122–123  
  overview, 120–121  
  revenue, 122  
accounts payable  
  defined, 85, 333  
  Operating activities section, statement of cash flows, 111  
  as undervalued liability, 310–311  
Accounts payable account, 52  
accounts payable turnover ratio, 220–221  
accounts receivable  
  current assets, 79  
  defined, 333  
  improving cash flow with collection of, 226–228  
  monitoring, 302–303  
  Operating activities section, statement of cash flows, 110  
  overstated assets, 308–309  
  when company's in trouble, 331  
Accounts receivable account, 50  
accounts receivable aging schedule, 218–219  
accounts receivable turnover ratio, 215–218  
accrual accounting, 42, 43–44, 333  
accrued expenses payable, 311  
accrued liabilities, 85–86, 333  
Accrued payroll taxes account, 52  
accumulate rating, 275  
accumulated amortization, 48  
accumulated depreciation, 47–48, 84  
Accumulated depreciation account, 50  
acid test ratio (quick ratio), 171–173  
acquisitions  
  consolidated financial statements, 147  
  diluted, 147  
  informing shareholders regarding, 285  
  notes to financial statements, 127–128  
  when company's in trouble, 331  
Actual amount column, internal budget report, 200  
actuary, 129  
Adelphia, 319–320  
adjusting sales  
  allowances, 96  
  overview, 95–96  
  returns, 96  
  tracking trends, 96–97  
  volume discounts, 96  
advertising  
  expenses and, 123  
  exploitation of cost, 304

- Advertising and promotion expense line item, income statement, 99
- affiliates, 84
- AICPA (American Institute of Certified Public Accounts), 242
- AIMR (Association for Investment Management and Research), 138
- allowances, 96
- American Institute of Certified Public Accounts (AICPA), 242
- amortization
  - defined, 48, 333
  - depreciation and, 47–48
  - expenses, 55
- analyst calls
  - determining employee satisfaction, 290
  - earnings expectations report, 288–289
  - hockey stick, 287
  - judging confidence of executive, 290
  - know when to expect, 290–291
  - lumpy sales, 287
  - mood of analyst, 289
  - overview, 276, 286–288
  - revenue growth report, 289
  - run-rate, 287
- analysts
  - bond, 272
  - buy-side, 268–269
  - corporation communication with, 276–277
  - independent, 271–272
  - overview, 267–268
  - sell-side, 269–271
  - use of financial report, 10
- angel investor, 30
- annual interest rate, 223–224
- annual meeting, shareholders', 280–281
- annual report
  - auditors' report section, 15, 66–69
  - balance sheet section, 16
  - capital resources, 65
  - company leaders, 62
  - corporate message, 61–62
  - financial statements section, 15, 70
  - highlights section, 15, 71
  - income statement section, 16
  - letter from president/CEO section, 15, 60–61, 66
  - liquidity, 66
  - management's discussion and analysis section, 15, 62–65
  - notes to the financial statements section, 12, 15, 71–72
  - overview, 12, 59–60, 284–285
  - public companies, 35
  - statement of cash flows section, 17
  - statement of shareholders' equity, 62
- annuity, 129
- arm's-length transaction, 300, 333
- Arthur Andersen
  - auditor for Enron, 318
  - auditor for Halliburton, 324
  - auditor for Sunbeam, 321–322
  - auditor for Waste Management, 323
  - scandal, 325
- artwork, as overstated asset, 310
- asset accounts
  - intangible assets, 51
  - overview, 49
  - tangible assets, 50–51
- assets
  - current, 16, 78–81
  - defined, 8, 333
  - exploitation of cost, 306–307
  - GAAP and IFRS standards, 263–264
  - intangible, 51, 336
  - long-term, 16, 81–84, 337
  - net, 337
  - overstated, 308–310
  - tangible, 50–52, 340
  - valuing, 134
  - when company's in trouble, 330
- associates, defined, 138
- Association for Investment Management and Research (AIMR), 138
- audit report, 240
- auditing
  - auditors, 237–240
  - certified public accountant, 236–237
  - corporate governance, 282
  - defined, 333
  - fraudulent financial reporting, 236

- generally accepted accounting principles, 240–243
  - overview, 235–236
  - auditors
    - audit report, 240
    - fieldwork, 238–240
    - overview, 237
    - preliminary review, 238
  - auditors' report section, annual report, 15, 66–69, 333
  - average costing inventory system, 80–81, 204, 207
- B •**
- balance sheet
    - account format, 76
    - accumulated depreciation, 84
    - assets, 78–84
    - dates, 74–75
    - defined, 16, 70, 334
    - equity, 86–88
    - financial position format, 77
    - GAAP and IFRS standards, 262
    - liabilities, 85–86
    - numbers, 76
    - overview, 73–74
    - report format, 77
  - basic earnings per share, income statement, 104
  - basic EPS, 154
  - beginning inventory, 200
  - Belnick, Mark, 322
  - big-bath charges, 295
  - bill payments, delaying to increase cash flow, 225–226
  - bill-and-hold transactions, 300–301
  - Bizstats website, 211
  - Blodget, Henry, 270
  - board of directors
    - compensation packages, 281
    - composition of, 281
    - negotiating with shareholders, 284
    - proxy votes, 283
    - reviewing audits, 282
    - takeover defenses and protections, 282
  - board operations, 253–255
  - bond analysts, 272
  - bond ratings, 274
  - bond-rating agencies, 272–275
  - bonds
    - defined, 87
    - junk, 273
    - long-term, 124
    - medium-term, 124
  - Bonds payable account, 52
  - borrowing options, to increase cash flow, 230–231
  - bottom line, 44
  - bottom-up budgeting, 194
  - BP, 132
  - Bristol-Meyers Squibb, 323
  - Budget amount column, internal budget report, 200
  - budgeting
    - approaches to, 194–195
    - cash budget, 199
    - direct labor budget, 198
    - direct materials budget, 198
    - internal reports, 201–202
    - inventory purchases budget, 198
    - master budget, 198–199
    - monthly reports, 199–201
    - overview, 193
    - production budget, 198
    - sales budget, 197–198
    - selling and administrative expense budgets, 198
    - setting goals, 195–197
  - Buildings account, 50
  - Buntrock, Dean, 323
  - businesses. *See also specific types of businesses*
    - corporations, 23–26
    - limited liability company, 22–23
    - partnerships, 21–22
    - sole proprietorship, 19–20
  - buying up companies, 142–144
  - buy-side analysts, 268–269, 334



## C corporations

defined, 24, 334

reporting requirements, 26

taxes, 24–25

## calculating

cash flow from operations, 313

cost of goods sold, 206

current ratio, 170

debt to shareholders' equity, 175, 176

debt-to-capital ratio, 177

dividend payout ratio, 158–159

earnings per share, 103–104, 152–153

FIFO inventory system, 207–208

interest coverage ratio, 173–174

inventory turnover, 209–212

number of days in accounts payable ratio, 221

price/earnings ratio, 153–155

quick ratio, 172

return on assets, 162–163

return on equity, 163–164

return on sales, 161

## capital, 88

capital expenditures, 112, 334

capital gains, 159, 334

capital improvements, 106

capital leases, 126

capital markets, 260

capital resources, 65

cash. *See also* cash flow

free cash flow, 180–181

importance of, 109

overview, 78–79

public company control of, 34

raising, 29–30, 33

cash budget, 199

cash debt coverage ratio, 185–188

cash EPS, 157

cash equivalents, 116–117

## cash flow

accounts payable turnover ratio, 220–221

accounts receivable aging schedule, 218–219

accounts receivable turnover ratio, 215–218

borrowing options, 230–231

cash debt coverage ratio, 185–188

cash flow coverage ratio, 188–190

cash return on sales ratio, 182–183

current cash debt coverage ratio, 183–185

defined, 8, 334

delaying bill payments to increase, 225–226

discount offers, 222–224

free cash flow, 180–181

improving collection of accounts

receivables, 226–228

number of days in accounts payable ratio, 221–222

overview, 179

receivables securitization program, 228–229

reducing inventory to improve, 229–230

when company's in trouble, 328

cash flow coverage ratio, 188–190

cash flow from operations

calculating, 313

defined, 334

Cash in checking account, 50

Cash in savings account, 50

Cash on hand account, 50

cash return on sales ratio, 182–183

cash-basis accounting, 42, 43–44, 334

cash-equivalent accounts, 180, 334

CEO (chief executive officer)

analyst calls, 276, 287

annual report, 60

letter for annual report, 15, 60–61, 66

pay raises, 282

responsibility regarding audit report, 66

certified public accountant (CPA), 11, 236–237

CFO (chief financial officer)

analyst calls, 276, 287

responsibility regarding audit report, 66

channel stuffing, 299

Chart of Accounts

asset accounts, 49–51

defined, 334

equity accounts, 52–53

expense accounts, 54–55

liability accounts, 52

- overview, 48–49
  - revenue accounts, 53–54
- Chartered Financial Analyst, 267
- chief executive officer. *See* CEO
- chief financial officer. *See* CFO
- Chinese Wall, 270
- Citigroup, 319
- class-action lawsuits, 285
- collectibility of revenue, 122
- collection period, 227
- common stock, 87, 334
- common stock account, 53
- companies. *See also* corporations;  
profitability of company; shareholders
  - buying up, 142–144
  - global, 13
  - private, 11, 27–30, 37–39
  - public, 11, 30–39
  - ranking with return on assets, 163
  - worldwide financial standard and, 260
- company leaders, 62
- company operations, 64–65
- compensation packages, 281
- competitors, use of financial report, 10
- compliance, financial reporting, 251–253
- concept release, 259
- confidentiality, private companies, 28–29
- consolidated financial statements
  - buying up companies, 142–144
  - defined, 334
  - GE, 138–142
  - notes, 146–148
  - overview, 137–138
  - reading, 144–146
- contingent liabilities, 312, 334
- convertibles, 104, 334
- cookie jar reserves, 296
- cooking the books. *See* creative accounting
- cooling-off period, 39
- corporate actions
  - acquisitions, 285
  - class-action lawsuits, 285
  - dividends, 285
  - mergers, 285
  - SEC investigation, 285
  - stock split, 285–286
- corporate governance
  - audits, 282
  - board of directors composition, 281
  - compensation packages, 281
  - composition of board of directors, 281
  - defined, 334
  - negotiating with shareholders, 284
  - proxy votes, 283
  - takeover defenses and protections, 282
- corporate message, annual report, 61–62
- corporations. *See also* companies
  - C corporation, 24–25, 26, 334
  - communication with analysts, 276–277
  - defined, 2
  - incorporation process, 23
  - reporting requirements, 25–26
  - S corporation, 24
  - taxes, 24
- Cost less accumulated depreciation line item, income statement, 121
- cost of goods sold
  - calculating, 206
  - considering, 97–98
  - defined, 335
  - inventory valuation methods and, 203–204, 205
- cost overruns, 324
- cost-plus contracts, 324
- costs. *See also* expenses
  - defined, 8
  - public companies, 34
  - Sarbanes-Oxley Act of 2002, 36–37
- CPA (certified public accountant), 11, 236–237
- creative accounting
  - big-bath charges, 295
  - cookie jar reserves, 296
  - creative acquisition accounting, 295–296
  - defining scope of problem, 294–295
  - discontinued operations, 312–313
  - expense recognition, 304–307
  - income taxes paid, 313–314
  - materiality, 296
  - overstated assets, 308–310
  - overview, 293–294
  - revenue recognition, 296, 297–304
  - undervalued liabilities, 310–312

creative acquisition accounting, 295–296

credit

amortization, 48

depreciation, 47–48

double-entry accounting, 45

effect on sales, 46–47

overview, 44–45

profit and loss statement, 46

using to increase cash flow, 230–231

Credit card payable account, 52

credit period, 226

credit policy, 218

credit standards, 226–227

Credit Suisse First Boston, 270

creditors, use of financial report, 9

current assets

accounts receivable, 79

Accounts receivable account, 50

cash, 78–79

Cash in checking account, 50

Cash in savings account, 50

Cash on hand account, 50

defined, 16, 335

inventory, 80–81

Inventory account, 50

marketable securities, 79–80

current cash debt coverage ratio, 183–185

current debt, 124

current liabilities

accounts payable, 85

Accounts payable account, 52

accrued liabilities, 85–86

Accrued payroll taxes account, 52

Credit card payable account, 52

current portion of long-term debt, 85

defined, 16, 335

Sales tax collected account, 52

short-term borrowings, 85

current P/E ratio, 153

current portion of long-term debt, 85

current ratio, 170–171

customers

nonpaying, 64

sales returns and allowances, 54

slow-paying, 332

top, 131

## • D •

dates, income statement, 90–91

debits

amortization, 48

depreciation, 47–48

double-entry accounting, 45

effect on sales, 46–47

overview, 44–45

profit and loss statement, 46

debt

current, 124

financing activities section, statement of

cash flows, 114–115

long-term, 86, 124–126, 337

short-term, 126, 339

when company's in trouble, 329–330

debt funding, 163

debt ratios, 127

debt to shareholders' equity, 174–176

debt-to-capital ratio, 176–178

defined benefit plan, retirement, 129

defined contribution plan, retirement, 129

depreciation

accounting policies note, 121–122

accumulated, 47–48, 84

amortization and, 47–48

defined, 335

expenses, 55

Operating activities section, statement of

cash flows, 109–110

Depreciation and amortization expenses

line item, income statement, 100

Difference column, internal budget

report, 200

diluted acquisitions, 147

diluted earnings per share, income

statement, 104

diluted EPS, 154

direct labor budget, 198

direct materials budget, 198

direct method, statement of cash flows,

107–108

direct stock purchase plans, 292

direct-response advertising, 304

- disclosure, public companies, 34
- discontinued operations
- cash flow and, 312–313
  - consolidated financial statements, 148
  - defined, 133, 335
  - GAAP and IFRS standards, 265
  - overview, 115–116
- discount offers, 222–224
- discount programs, to improve cash flow, 227
- discount rate, pension obligations, 130
- discretionary cash (free cash flow), 180–181
- Disney, Roy, 282
- dividend payout ratio
- calculating, 158–159
  - companies with best, 160
  - importance of, 159–160
  - overview, 158
- dividend reinvestment plans, 292
- dividends
- defined, 87, 335
  - financing activities section, statement of cash flows, 114
  - informing shareholders, 285
- Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, 274, 294
- double-entry accounting, 8, 45, 335
- Dow Corning, 132
- drawing account, 88
- Dunlap, Albert, 321
- durable goods, 335
- **E** ●
- earnings
- managed, 295, 297
  - restating, 294
- earnings before interest and taxes (EBIT), 56
- earnings before interest, taxes, depreciation, and amortization (EBITDA), 56, 101–102, 157, 335
- earnings expectations report, 288–289
- earnings per share (EPS)
- basic, 154
  - calculating, 103–104, 152–153
  - cash, 157
  - defined, 335
  - diluted, 154
  - headline, 157
  - pro forma, 157
  - reported, 157
- Earningscast website, 291
- Ebbers, Bernard, 320
- EBIT (earnings before interest and taxes), 56
- EBITDA (earnings before interest, taxes, depreciation, and amortization), 56, 101–102, 157, 335
- economic viability, 305
- effective date, stock offering, 39
- 8-K form, 13, 251–253
- Eisner, Michael, 279, 282, 284
- electronic bill payment, 231
- Emerging Issues Task Force, 14
- employees
- determining satisfaction, 290
  - suspension of benefit plans, 253
  - use of financial report, 9
- ending inventory's value, 205, 206
- Enron, 282, 283, 318
- Enron Creditors Recovery Corporation, 318
- environmental concerns, 132
- EPS (earnings per share)
- basic, 154
  - calculating, 103–104, 152–153
  - cash, 157
  - defined, 335
  - diluted, 154
  - headline, 157
  - pro forma, 157
  - reported, 157
- Equipment account, 51
- equity
- capital, 88
  - defined, 8, 335
  - drawing, 88
  - retained earnings, 87
  - stock, 86–87



- equity accounts
    - common stock, 53
    - overview, 52–53
    - preferred stock, 53
    - retained earnings, 53
  - Excess of expenses over revenues report, 90
  - Excess of revenues over expenses report, 90
  - Executive Pay Watch database, 282
  - executives. *See also* CEO
    - judging confidence of, 290
    - use of financial report, 9
  - expectations, budgeting process, 193
  - expense accounts, 54–55
  - expenses. *See also* costs
    - accounting policies note, 122–123
    - advertising, 99, 304
    - asset impairment, 306–307
    - defined, 335
    - interest, 336
    - licenses, 305–306
    - patents, 305–306
    - research and development, 305
    - restructuring charges, 307
  - extended reporting period, 298–299
  - Exxon, 132
- F •**
- Fair Disclosure Rule (Regulation FD), 276, 286
  - FASB (Financial Accounting Standards Board)
    - changes in accounting policies, 134–135
    - changing principles, 242–243
    - defined, 335
    - formation of, 14
    - generally accepted accounting principles, 241
    - income statement, 90
    - Norwalk Agreement, 258
    - overview, 242
    - segment reporting, 146
  - Fastow, Andrew S., 318
  - fees, improving cash flow with, 227
  - fictional sales, 299
  - fieldwork, auditors, 238–240
  - FIFO (first in, first out) inventory system
    - calculating, 207–208
    - defined, 80, 204
    - GAAP and IFRS standards, 264–265
  - Financial Accounting Standards Board. *See* FASB
  - financial commitments
    - leases, 126–127
    - long-term debt, 124–126
    - short-term debt, 126
  - financial freedom, of private companies, 29
  - financial information section, Form 10-Q, 246
  - financial position format, balance sheet, 77
  - financial reporters, use of financial report, 10
  - financial reporting. *See also* reports
    - defined, 7
    - history of, 14
  - financial statements
    - defined, 335
    - GAAP and IFRS standards, 261–263
  - financial statements section, annual report, 15, 70
  - financing activities section, statement of cash flows
    - buying back stock, 113–114
    - incurring new debt, 114–115
    - issuing stock, 113
    - overview, 106
    - paying dividends, 114
    - paying off debt, 115
  - finished-goods inventory, 97
  - Fiorina, Carly, 283
  - first in, first out (FIFO) inventory system
    - calculating, 207–208
    - defined, 80, 204
    - GAAP and IFRS standards, 264–265
  - Fitch, John Knowles, 273
  - Fitch Publishing Company, 273
  - Fitch Ratings, 273
  - fixed assets
    - gains and losses from, 314
    - turnover, 212–213
  - fixed costs
    - defined, 335
    - gauging gross profit, 98
  - flexibility, of private companies, 29



- foreign currency exchange, 116
- forms
- Form 8-K, 13, 251–253
  - Form 10-K, 12, 247–250
  - Form 10-Q, 246–247
  - Form 1065, 20
  - internal ownership, 256
  - Schedule C (Profit or Loss from Business), 20
  - Schedule C-EZ (Net Profit from Business), 20
  - Schedule K-1 (Partner's Share of Income, Credits, Deductions, Etc.), 20
  - Schedule SE (Self-Employment Tax), 20
- forward P/E ratio, 153
- fraudulent financial reporting, 236, 336
- free cash flow (discretionary cash), 180–181
- Freight charges account, 54
- Furniture and Fixtures account, 51
- **G** •
- GAAP (generally accepted accounting principles)
- accounting framework, 261
  - accrual accounting, 42
  - assets, 263–264
  - auditing process, 240–243
  - defined, 336
  - discontinued operations, 265
  - filing statements according to, 17
  - financial statements, 261–263
  - impairment charges, 265–266
  - inventory, 264–265
  - private companies, 11
  - pro forma EPS, 157
  - recognition of, 14
  - related-party transactions, 265
  - revenue recognition, 261–263
- gains
- from fixed assets, 314
  - from investments, 314
  - unrealized, 340
- GE (General Electric), 138–142, 146–147
- General Electric Capital Corporation (GECC), 146
- general ledger, 48
- General office needs expense line item, income statement, 99
- generally accepted accounting principles.  
*See* GAAP
- global companies, reports, 13
- global financial reporting
- capital markets, 260
  - companies, 260
  - GAAP versus IFRS, 261–266
  - investors, 259–260
  - overview, 257–258
  - reshaping, 258–259
- goals, budgeting, 195–197
- going-concern problem, 69, 336
- goods ordered but not shipped, 298
- goods shipped but not ordered, 298
- goodwill account
- consolidated financial statements, 148
  - defined, 51, 336
  - overview, 128
  - testing, 306–307
- government. *See also* forms
- board operations, 253–255
  - compliance with regulations, 251–253
  - insider ownership regulations, 255–256
  - overview, 245–246
  - report on internal controls, 250–251
  - reports for, 12–13
  - use of financial report, 9
- gross margin, 165, 336
- gross profit, 55–56, 336
- Gross profit line, income statement, 92, 98
- **H** •
- Halliburton, 324
- Hasbro
- accounts payable turnover ratio, 220–221
  - accounts receivable turnover ratio, 217–218
  - calculating current ratio, 170
  - calculating debt to shareholders' equity, 176
  - calculating debt-to-capital ratio, 177
  - calculating interest coverage ratio, 174
  - calculating quick ratio, 172
  - cash debt coverage ratio, 187
  - cash flow coverage ratio, 190
  - cash on hand, statement of cash flows, 117
  - cash return on sales ratio, 183

Hasbro (*continued*)

consolidated financial statements, 138  
 current cash debt coverage ratio, 185  
 dividend payout ratio, 159  
 earnings per share, 154–155  
 Effect of currency exchange rate changes  
   on cash, 116  
 financing activities section, statement of  
   cash flows, 115  
 fixed assets turnover, 212  
 free cash flow, 181  
 gross margin, 165  
 inventory turnover, 211–212  
 long-term debt, 125  
 net profit margin, 168  
 number of days in accounts payable  
   ratio, 222  
 operating activities section, statement of  
   cash flows, 112  
 operating margin, 166  
 return on equity, 164  
 return on sales, 161–162  
 short-term debt, 126  
 total asset turnover, 213

Hau, Thomas, 323  
 headline EPS, 157  
 Hewlett, Walter, 283  
 Hewlett-Packard, 283  
 highlights section, annual report, 15, 71  
*History of Railroads and Canals of the  
 United States* (Poor), 273  
 hockey stick, revenue, 287  
 hold rating, 275



IASB (International Accounting Standards  
 Board), 14

IFRS (International Financial Reporting  
 Standards)

assets, 263–264  
 development of, 13  
 discontinued operations, 265  
 financial statements, 261–263  
 versus GAAP, 261–266  
 impairment charges, 265–266  
 inventory, 264–265

related-party transactions, 265  
 revenue recognition, 261–263  
 impairment charges, 265–266  
 incentives  
   sales, 44  
   stock, 64  
 Income before taxes line, income  
   statement, 92  
 Income from operations line, income  
   statement, 92  
 income statement  
   cost of goods sold number, 203  
   dates, 90–91  
   defined, 16, 46, 336  
   earnings per share, 103–104  
   expenses, 99–100  
   GAAP and IFRS standards, 262  
   multistep format, 92–93  
   overview, 70, 89–90  
   profits, 101–103  
   revenue, 92–98  
   single-step format, 91–92  
 income taxes, 313–314  
 incorporation process, 2  
 independent analysts, 271–272  
 indirect method, statement of cash flows,  
   107–108  
 initial public offering. *See* IPO  
 in-process research and development, 296  
 insider ownership, 255–256  
 insolvent, 336  
 in-store credit, 216, 336  
 Insurance expenses line item, income  
   statement, 100  
 intangible assets  
   defined, 336  
   goodwill, 51  
   intellectual property, 51  
 intellectual property, 51, 336  
 interest coverage ratio, 173–174  
 interest expenses, 55, 100, 336  
 internal budget reports, 201–202  
 internal controls, 239, 250–251  
 internal financial report, 10, 13–14,  
   199–202, 337  
 International Accounting Standards Board  
   (IASB), 14

International Financial Reporting Standards. *See* IFRS

introductory paragraph, auditors' report, 67

inventory

- fixed assets turnover, 212–213
- GAAP and IFRS standards, 264–265
- Operating activities section, statement of cash flows, 110
- overstated assets, 309
- reducing to improve cash flow, 229–230
- total asset turnover, 213–214
- tracking, 80–81, 205
- turnover, 209–211
- valuation methods, 203–209
- when company's in trouble, 328

Inventory account, 50

inventory purchases budget, 198

inventory turnover

- calculating, 209–212
- when company's in trouble, 331

investing activities section, statement of cash flows, 106, 112–113

investment bankers, 38

investments

- gains and losses from, 314
- price/earnings ratio and, 156

Investor Calendar website, 276

investors

- angel, 30
- bankers, 38
- use of financial report, 9
- venture capitalist, 30
- worldwide financial standard and, 259–260

IPO (initial public offering)

- defined, 31, 113, 336
- failed, 34

## • J •

Jobs, Steve, 32

joint ventures, 138

junk bonds, 273

just-in-time inventory system, 229

## • K •

Kersh, Russell, 321

Koenig, James, 323

Kozlowski, L. Dennis, 322

## • L •

Land account, 50

last in, first out (LIFO) inventory system, 80, 204, 208–209, 264–265

late payments, improving cash flow with, 227

lawsuits

- Arthur Andersen, 322, 323, 325
- class-action, 285
- contingent liabilities and, 312
- Dow Corning, 132
- as red flag, 133

Lay, Kenneth L., 318

LCM (lower of cost or market) inventory system, 81, 204

leading (projected) P/E ratio, 153

Leasehold improvements account, 51

leases, 126–127

letter from president/CEO section, annual report, 15, 60–61, 66

leverage, 175

leveraged buyout, 102

Levitt, Arthur, 295, 296

liabilities

- accrued, 85–86, 333
- cash debt coverage ratio and, 185–186
- contingent, 312, 334
- current, 16, 52, 85–86, 335
- defined, 8, 337
- long-term, 16, 52, 86, 337
- pay-down, 312
- undervalued, 310–312
- valuating, 134
- when company's in trouble, 330

liability accounts, 52

licenses

- CPA, 236–237
- exploitation of cost, 305–306

LIFO (last in, first out) inventory system, 80, 204, 208–209, 264–265

- limited liability company (LLC), 22–23
  - Line item column, internal budget report, 199
  - lines of credit, 230–231
  - liquidations, 148
  - liquidity
    - annual report, 66
    - current ratio, 170–171
    - debt to shareholders' equity, 174–176
    - debt-to-capital ratio, 176–178
    - defined, 337
    - interest coverage ratio, 173–174
    - overview, 169
    - public companies, 33, 34
    - quick ratio, 171–173
    - when company's in trouble, 327
  - LLC (limited liability company), 22–23
  - Loans payable account, 52
  - lockbox services, 231
  - long-term assets
    - Accumulated depreciation account, 50
    - Buildings account, 50
    - capitalized leases, 82
    - defined, 16, 337
    - Equipment account, 51
    - Furniture and fixtures account, 51, 82–83
    - intangible assets, 83
    - Land and buildings account, 50, 81–82
    - Leasehold improvements account, 51, 82
    - Machinery and equipment accounts, 82
    - Other assets account, 83–84
    - tools, dies, and molds, 83
    - Vehicles account, 51
  - long-term debt, 86, 124–126, 337
  - long-term liabilities
    - Bonds payable account, 52
    - defined, 16, 337
    - Loans payable account, 52
    - overview, 86
  - long-term notes/bonds, 124
  - losses
    - defined, 8
    - from fixed assets, 314
    - from investments, 314
    - net, 103
    - unrealized, 340
  - lower of cost or market (LCM) inventory system, 81, 204
  - lumpy sales, 287
- M •
- Madoff, Bernard, 319
  - majority interest, 143, 337
  - managed earnings, 295, 297
  - management fees, 145
  - management's discussion and analysis (MD&A) section, annual report
    - company operations, 64–65
    - defined, 15
    - overview, 62–64
  - managers, use of financial report, 9
  - managing earnings, 337
  - market value, 155–156
  - marketable securities
    - current assets, 79–80
    - defined, 337
  - Mars, Ethel, 28
  - Mars, Frank, 28
  - Mars company, 28
  - master budget, 198–199
  - material changes, 337
  - material misstatement, 337
  - materiality, 296
  - Mattel
    - accounts payable turnover ratio, 220
    - accounts receivable turnover ratio, 216–217
    - calculating current ratio, 170
    - calculating debt to shareholders' equity, 175
    - calculating debt-to-capital ratio, 177
    - calculating interest coverage ratio, 173–174
    - calculating quick ratio, 172
    - cash debt coverage ratio, 186–187
    - cash flow coverage ratio, 189
    - cash on hand, statement of cash flows, 117
    - cash return on sales ratio, 182
    - consolidated financial statements, 138
    - current cash debt coverage ratio, 184

- dividend payout ratio, 158–159
  - earnings per share, 154–155
  - Effect of currency exchange rate changes
    - on cash, 116
  - financing activities section, statement of
    - cash flows, 115
  - fixed assets turnover, 212
  - free cash flow, 180–181
  - gross margin, 165
  - inventory turnover, 210–211
  - long-term debt, 125
  - net profit margin, 167–168, 182
  - number of days in accounts payable
    - ratio, 222
  - operating activities section, statement of
    - cash flows, 112
  - operating margin, 166
  - recalls, 123
  - return on assets, 162–163
  - return on equity, 163–164
  - return on sales, 161–162
  - short-term debt, 126
  - total asset turnover, 213
  - MD&A (management's discussion and analysis) section, annual report
    - company operations, 64–65
    - defined, 15
    - overview, 62–64
  - medium-term notes/bonds, 124
  - merchant services, 231
  - mergers
    - consolidated financial statements, 147
    - informing shareholders, 285
    - notes to financial statements, 127–128
    - when company's in trouble, 331
  - Merrill Lynch, 270
  - Microsoft
    - paying dividends, 159
    - price/earnings ratio, 156
  - Milky Way bar, 28
  - minority interest, stock acquisition, 143
  - mobile apps, communicating via, 277
  - monthly budget reports, 199–201
  - mood of analyst, 289
  - Moody, John, 273
  - Moody's Investor Service, 273
  - Morgan Stanley Dean Witter & Co., 270
  - Morningstar website, 269, 272
  - Mulcahey, Michael, 320
  - multistep format, income statement, 92–93
- N •
- NASDAQ, 38
  - negative working capital, 171
  - net assets, 77, 337
  - net business income, 20, 337
  - net income, 204
  - Net income (Net loss) line, income statement, 92
  - net loss, 92, 103
  - net marketable value, 337
  - net profit, 56, 103, 167–168, 182, 337
  - Net Profit from Business (Schedule C-EZ) form, 20
  - net revenue, 337
  - net sales, 337
  - New York Stock Exchange (NYSE), 14, 38
  - nominating process, board members, 254–255
  - noncurrent assets, 77
  - nonoperating income, 102–103, 337
  - nonstandard auditors' report, 67–68
  - Norwalk Agreement, 258
  - notes
    - long-term, 124
    - medium-term, 124
  - notes to financial statements
    - accounting policies, 120–123
    - defined, 12, 338
    - financial commitments, 124–127
    - mergers and acquisitions, 127–128
    - overview, 119
    - pension and retirement benefits, 128–130
    - reading, 71–72
    - red flags, 133–135
    - reviewing revenue-recognition policies, 301–302
    - segment breakdowns, 130–132
    - significant events, 132–133

number of days in accounts payable ratio  
 calculating, 221  
 Hasbro, 222  
 Mattel, 222  
 numbers, rounding, 76  
 NYSE (New York Stock Exchange), 14, 38

## • 0 •

off-the-books partnerships, 318  
 1065 Form, 20  
 Operating activities section, statement of  
 cash flows  
 accounts payable, 111  
 accounts receivable, 110  
 depreciation, 109–110  
 inventory, 110  
 overview, 106  
 operating cash flow, 157, 338  
 operating expenses, 55, 338  
 operating leases, 126, 338  
 operating margin, 165–167, 338  
 operating period, 90–91, 338  
 operating profit, 56, 338  
 opinion paragraph, auditors' report, 67  
 Other expenses line item, income  
 statement, 100  
 Other selling administration expenses line  
 item, income statement, 39  
 overstated assets  
 accounts receivable, 302–309  
 artwork, 310  
 inventory, 309  
 undeveloped land, 310  
 owner diversification, public  
 companies, 33  
 Owner's equity account, 52

## • P •

P&L (profit and loss) statement  
 cost of goods sold number, 203  
 dates, 90–91  
 defined, 16, 46, 336  
 earnings per share, 103–104

expenses, 99–100  
 GAAP and IFRS standards, 262  
 multistep format, 92–93  
 overview, 70, 89–90  
 profits, 101–103  
 revenue, 92–98  
 single-step format, 91–92  
 Pacioli, Luca, 14  
 parent company  
 defined, 138, 338  
 transactions to eliminate when preparing  
 consolidated financial statements,  
 144–146  
 Partner's Share of Income, Credits,  
 Deductions, Etc. (Schedule K-1)  
 form, 20  
 partnerships  
 defined, 332  
 overview, 21  
 reporting requirements, 22  
 taxes, 21  
 patents, 305–306  
 pay-down liabilities, 312  
 PCAOB (Public Company Accounting  
 Oversight Board), 36  
 P/E (price/earnings) ratio  
 calculating, 153–155  
 earnings per share, 152–153  
 judging company market value with,  
 155–156  
 overview, 152  
 variations, 156–158  
 pensions, 128–130  
 periodic inventory tracking, 205  
 perpetual inventory system, 205  
 physical capacity  
 assessing, 303  
 defined, 338  
 Ponzi scheme, 319  
 Poor, Henry Varnum, 273  
 preferred stock, 53, 87, 338  
 preliminary review, auditors, 238  
 president. *See also* CEO  
 analyst calls, 287  
 annual report, 60  
 letter for annual report, 15, 60–61, 66

- press releases, 277  
press reports, 277  
price/earnings ratio. *See* P/E ratio  
PricewaterhouseCoopers website, 261  
Prince, Charles, 319  
private companies  
  advantages of, 28–29  
  converting to public companies, 37–39  
  disadvantages of, 29–30  
  overview, 27–28  
  reporting requirements, 30–31  
  reports for, 11  
pro forma EPS, 157  
product development, 122–123  
production budget, 198  
profit and loss (P&L) statement  
  cost of goods sold number, 203  
  dates, 90–91  
  defined, 16, 46, 336  
  earnings per share, 103–104  
  expenses, 99–100  
  GAAP and IFRS standards, 262  
  multistep format, 92–93  
  overview, 70, 89–90  
  profits, 101–103  
  revenue, 92–98  
  single-step format, 91–92  
profit margins  
  gross margin, 165, 336  
  net profit margin, 167–168  
  operating margin, 165–167  
  overview, 164–165  
  when company's in trouble,  
    328–329  
Profit or Loss from Business (Schedule C)  
  form, 20  
Profit or Loss from Farming  
  (Schedule F), 20  
profitability of company  
  dividend payout ratio, 158–160  
  gross profit, 336  
  price/earnings ratio, 152–158  
  profit margins, 164–168  
  return on assets, 162–163  
  return on equity, 163–164  
  return on sales, 161–162  
profits  
  defined, 8, 338  
  EBITDA, 101–102  
  gross, 55–56, 336  
  net, 56, 103, 167–168, 182, 337  
  nonoperating income, 102–103  
  operating, 56, 338  
  overview, 101  
projected (leading) P/E ratio, 153  
proxies, 338  
proxy votes, shareholders, 283  
public companies  
  advantages of, 33  
  converting private companies to, 37–39  
  disadvantages of, 34  
  overview, 31–33  
  reporting requirements, 35–37  
  reports for, 11  
Public Company Accounting Oversight  
  Board (PCAOB), 36  
Public Super Markets, 31  
Purchase discounts account, 54  
Purchase returns and allowances  
  account, 54  
Purchases account account, 54
- **Q** •
- qualified audit report, 67  
qualified opinion, 69  
quarterly report  
  overview, 11  
  public companies, 35  
quick ratio (acid test ratio), 171–173
- **R** •
- R&D (research and development), 100,  
  296, 305  
raising cash  
  private companies, 29–30  
  public companies, 33  
rate of compensation increases,  
  pensions, 130  
rate of return on assets, pensions, 130  
raw materials, 97



- Real World Example icon, 4
- receivables securitization program, 228–229
- receivership, 252, 338
- recognizing. *See also* revenue recognition
  - defined, 338
  - overstated assets, 308–310
  - revenue, 63, 296
  - special line items, 115–116
- Red flag column, internal budget report, 199
- red flags
  - auditors' report, 67
  - in notes to financial statements, 133–135
- red herring, 39
- Regulation FD (Fair Disclosure Rule), 276, 286
- reinvestment plans
  - direct stock purchase plans, 292
  - dividend reinvestment plans, 292
  - overview, 291
- related-party revenue
  - defined, 300, 338
  - GAAP and IFRS standards, 265
- Remember icon, 4
- report format, balance sheet, 77
- reported EPS, 157
- reporting requirements
  - corporations, 25–26
  - limited liability company, 23
  - private companies, 30–31
  - public companies, 35–37
  - sole proprietorship, 19–20
- reports. *See also* annual report
  - annual, 12, 15–17
  - budgeting, 199–202
  - global companies, 13
  - government requirements, 12–13
  - importance of, 9–10
  - internal, 10, 13–14, 199–202, 337
  - overview, 7–8
  - preparing, 8
  - for private companies, 11
  - for public companies, 11
  - quarterly, 11, 35
  - readers of, 9–10
  - research and development (R&D), 100, 296, 305
- Research and product development expense line item, income statement, 100
- restating earnings, 294, 339
- restructuring
  - charges, 307
  - defined, 133, 339
- retained earnings, 159, 309, 339
- retained earnings account, 53, 87
- retirement benefits, 128–130
- return on assets. *See* ROA
- return on equity. *See* ROE
- return on sales. *See* ROS
- returns, 96
- revenue
  - accounting policies note, 122
  - adjusting sales, 95–97
  - cost of goods sold, 97–98
  - defined, 94–95, 339
  - gross profit, 98
  - hockey stick, 287
  - net, 337
  - when company's in trouble, 329
- revenue accounts
  - cost of goods sold, 54
  - sales discounts, 53–54
  - sales of goods or services, 53
  - sales returns and allowances, 54
- revenue growth report, 289
- revenue recognition
  - assessing physical capacity, 303
  - bill-and-hold transactions, 300–301
  - channel stuffing, 299
  - defined, 296
  - evaluating revenue results, 302
  - extended reporting period, 298–299
  - fictional sales, 299
  - GAAP and IFRS standards, 261–263
  - goods ordered but not shipped, 298
  - goods shipped but not ordered, 298
  - monitoring accounts receivable, 302–303
  - overview, 297
  - related-party revenue, 300
  - reviewing policies, 301–302

rights of return, 300  
side letters, 299–300  
up-front service fees, 301  
riding the trade (stretching accounts payable), 225  
Rigas, John, 319–320  
Rigas, Michael, 320  
Rigas, Timothy, 320  
rights of return, 300  
ROA (return on assets)  
  calculating, 162–163  
  overview, 162  
  ranking companies with, 163  
road shows, 39, 277  
ROE (return on equity)  
  calculating, 163–164  
  overview, 163  
  role in determining profitability, 164  
Rooney, Phillip, 323  
ROS (return on sales)  
  calculating, 161  
  overview, 161  
  role in determining profitability, 162  
royalties, 99–100, 339  
run-rate, 287

• S •

S corporation  
  defined, 24  
  taxes, 24  
S&P (Standard & Poor's), 272, 273  
sales  
  adjusting, 95–97  
  defined, 8  
  effect of debits and credits on, 46–47  
  fictional, 299  
  incentives, 44  
  lumpy, 287  
  net, 337  
  sales budget, 197–198  
  sales discounts account, 53–54  
  sales forecast, 196–197  
  sales of goods or services account, 53  
  sales price, 122  
  sales returns and allowances account, 54

Sales tax collected account, 52  
Sarbanes-Oxley Act of 2002, 36–37, 250, 251  
SBA (Small Business Administration)  
  loans, 231  
scandals, financial  
  Adelphia, 319–320  
  Arthur Andersen, 324  
  Bristol-Meyers Squibb, 323  
  Citigroup, 319  
  Enron, 318  
  Halliburton, 324  
  Madoff, Bernard, 319  
  Sunbeam, 321–322  
  Tyco, 322  
  Waste Management corporation,  
    322–323  
  WorldCom/MCI, 320–321  
Schedule C (Profit or Loss from Business)  
  form, 20  
Schedule C-EZ (Net Profit from  
  Business) form, 20  
Schedule F (Profit or Loss from  
  Farming), 20  
Schedule K-1 (Partner's Share of Income,  
  Credits, Deductions, Etc.) form, 20  
Schedule SE (Self-Employment Tax)  
  form, 20  
scope paragraph, auditors' report, 67  
SEC (Securities and Exchange Commission)  
  Accounting and Auditing Enforcement  
    Releases, 314  
  arm's-length transaction, 300  
  audit requirements, 282  
  auditors, 237  
  changes in accounting policies, 134–135  
  concept release, 259  
  cooling-off period, 39  
  creating accounting techniques, 295–296  
  Edgar website, 245  
  Fair Disclosure Rule (Regulation FD),  
    276, 286  
  IFRS Road Map, 258  
  income statement, 90  
  management's discussion and analysis  
    section, annual report, 62–64  
  origin of, 14

SEC (*continued*)

- Public Company Accounting Oversight Board, 36
- reporting requirements, 11, 12–13
- Rule 10A-3, 284
- segment reporting, 146
- testing goodwill, 306–307
- secondary public offerings, 113, 339
- secured debt, 339
- secured debtors, 87
- secured line of credit, 231
- securities
  - defined, 339
  - marketable, 79–80, 337
  - trading, 340
- Securities and Exchange Act of 1934, 31
- Securities and Exchange Commission (SEC)
  - Accounting and Auditing Enforcement Releases, 314
  - arm’s-length transaction, 300
  - audit requirements, 282
  - auditors, 237
  - changes in accounting policies, 134–135
  - concept release, 259
  - cooling-off period, 39
  - creating accounting techniques, 295–296
  - Edgar website, 245
  - Fair Disclosure Rule (Regulation FD), 276, 286
  - IFRS Road Map, 258
  - income statement, 90
  - management’s discussion and analysis section, annual report, 62–64
  - origin of, 14
  - Public Company Accounting Oversight Board, 36
  - reporting requirements, 11, 12–13
  - Rule 10A-3, 284
  - segment reporting, 146
  - testing goodwill, 306–307
  - segment breakdowns, 130–132
  - segment reporting, 146
  - Self-Employment Tax (Schedule SE) form, 20
  - sell rating, 275
  - selling and administrative expense budgets, 198
  - sell-side analysts, 269–271
  - servicing rights, receivables, 228
  - shareholders
    - analyst calls, 286–291
    - annual meeting, 280–281
    - annual reports, 284–285
    - corporate actions, 285–286
    - corporate governance, 281–284
    - negotiating with, 284
    - proxy votes, 283
    - reinvestment plans, 291–292
    - use of company websites, 291
  - shareholders’ equity
    - defined, 339
    - return on assets and, 163
  - Shareholders’ equity account, 52
  - short-term borrowings, 85
  - short-term debt, 126, 339
  - short-term financing, 229
  - side letters, 299–300, 339
  - single-step format, income statement, 91–92
  - Skilling, Jeffrey, 318
  - Small Business Administration (SBA) loans, 231
  - sole proprietorship
    - defined, 339
    - overview, 19–20
    - reporting requirements, 19–20
    - taxes, 19
  - solvency
    - cash debt coverage ratio, 185–188
    - cash flow coverage ratio, 188–190
    - cash return on sales ratio, 182–183
    - current cash debt coverage ratio, 183–185
    - defined, 188–190, 339
    - free cash flow, 180–181
    - overview, 179
  - SoRIE (Statement of recognised income and expense), 262–263
  - special line items, statement of cash flows, 115
  - discontinued operations, 115–116
  - foreign currency exchange, 116

specific identification inventory system, 81, 204

Spitzer, Eliot, 270

Standard & Poor's (S&P), 272, 273

standard auditors' report, 67

statement of cash flows

- cash equivalents, 116–117
- defined, 17, 339
- direct method, 107–108
- financing activities section, 106, 113–115
- GAAP and IFRS standards, 263
- indirect method, 107–108
- investing activities section, 106, 112–113
- operating activities section, 106, 109–111
- overview, 70, 105–106
- special line items, 115–116

statement of changes in shareholder's equity, 62, 262–263

Statement of recognised income and expense (SoRIE), 262–263

statutory consolidation, 143

statutory merger, 143

stock

- common, 87
- financing activities section, statement of cash flows, 113–114
- overview, 86–87
- preferred, 87

stock acquisition, 143

stock incentives, 64, 339

stock market index, 273

stock option plans, 281, 339

stock ratings, 275

stock splits, 285–286

stretching accounts payable (riding the trade), 225

strong buy, 275

subsidiaries

- defined, 138
- transactions eliminated by parent company when preparing consolidated financial statements, 144–146

Sullivan, Scott, 320

Sunbeam, 321–322

Swartz, Mark, 322

## • T •

takeover defenses and protections, 282

tangible assets

- current assets, 50–51
- defined, 340
- long-term assets, 51–52

target markets, 131

tax liability account, 43, 340

taxes

- corporations, 24
- expense accounts, 55
- limited liability company, 22
- operating cash flow and, 313–314
- sole proprietorship, 19

Taxes expense line item, income statement, 100

Technical Stuff icon, 4

10-K form, 12, 247–250

10-Q form, 12, 246–247

theIRAPP app, 277

Tip icon, 3

Tobecksen, Bruce, 323

top-down approach, budgeting process, 194

total asset turnover, 213–214

tracking inventory, 205

trade financing, 225

trade sanctions, 131

trading securities, 80, 340

trailing P/E ratio, 153

turnover, inventory

- calculating, 209–210
- Hasbro, 211–212
- Mattel, 210–211

turnover ratio, 302

Tyco, 322

## • U •

unconsolidated subsidiary, 83–84

undervalued liabilities

- accounts payable, 310–311
- accrued expenses payable, 311
- contingent liabilities, 312
- pay-down liabilities, 312

underwriting guarantee, 38  
 undeveloped land, 310  
 unqualified audit report, 67  
 unrealized losses/gains, 340  
 unsecured line of credit, 230  
 up-front service fees, 301

## • U •

Valdez oil spill, 132  
 valuation methods, inventory  
   average costing system, 204  
   FIFO system, 80, 204, 207–208,  
     264–265  
   LIFO system, 80, 204, 208–209,  
     264–265  
   lower of cost or market system,  
     81, 204  
   specific identification system, 81, 204  
 value investing, 156  
 valuing  
   assets, 134  
   liabilities, 134  
 variable costs  
   defined, 340  
   gauging gross profit, 98  
 Vehicles account, 51  
 venture capitalist, 30, 340  
 venturers, 138  
 volume discount, 96, 340

## • W •

Wallstreet website, 276  
 Warning icon, 4  
 warrants, 104  
 Waste Management corporation, 322–323  
 weighted average, 152–153

wholly owned subsidiary, 143, 340  
 window dressing, 289  
 working capital, 77, 340  
 work-in-process inventory, 97  
 WorldCom/MCI, 320–321  
 worldwide financial standard  
   capital markets, 260  
   companies, 260  
   GAAP versus IFRS, 261–266  
   investors, 259–260  
   overview, 257–258  
   reshaping, 258–259  
 Wozniak, Steve, 32

## • Y •

Yahoo! Finance website, 156, 246, 256,  
 277, 291  
 yearly report  
   auditors' report section, 15, 66–69  
   balance sheet section, 16  
   capital resources, 65  
   company leaders, 62  
   corporate message, 61–62  
   financial statements section, 15, 70  
   highlights section, 15, 71  
   income statement section, 16  
   letter from president/CEO section, 15,  
     60–61, 66  
   liquidity, 66  
   management's discussion and analysis  
     section, 15, 62–65  
   notes to the financial statements section,  
     12, 15, 71–72  
   overview, 12, 59–60, 284–285  
   public companies, 35  
   statement of cash flows section, 17  
   statement of shareholders' equity, 62