



Quality of Earnings Case Study Collection

Edited by

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FOREWORD

“Earnings Quality” has been a subject of SEC investigations, articles in most, if not all, business publications, and significant debate in recent years. It is a matter of importance in the financial reporting and regulatory communities, and it impacts the confidence of investors in our financial markets. Considering that the U.S. controls 40% of the world’s capital markets, and you get an appreciation for the global economic impact that shaken investor confidence could have. For this reason, we have engaged authors and experts to assemble this collection of case studies, to put the reader in the seat of executives making decisions that could impact the future of their company, and their own and their employees livelihoods.

The concept of Quality of Earnings goes back to preparers understanding the economic substance of a transaction, then reflecting it properly in the books and records of the company. However, this is not always easy, as accounting rules are not simply black and white, and the nature of transactions is ever more complex. This understanding can be improved when the CFO, an expert in the management of process, technology and resources, is part of the decision-making process in a company and can help guide and shape decisions to make better sense within the context of GAAP and regulatory reporting requirements.

Managing the business and its operations to achieve a desired outcome or hit a target is entirely appropriate, (the emphasis here is placed on managing the business); managing earnings as we all agree, is not an acceptable practice to hit earnings targets. The AICPA will continue to provide guidance and education to ensure that our members, and others in the financial reporting community report high quality earnings and the necessary disclosures to enable the investing public to make better informed decisions.

One way to do this is through the creation of a robust performance measurement system incorporating both financial and non-financial measures that not only measure current positions but also are predictive of future conditions in the business. Knowing and understanding key metrics in a company can lead to better decision-making and reporting, and thus higher quality of earnings. Having an effective early-warning system in place could obviate the need for managing earnings by giving more of an opportunity for managing operations.

We hope you use these cases as an education opportunity for yourself and for your colleagues. You may want to create an interactive discussion session by distributing the cases for discussion, and then introducing the expert commentary for review. If you learn something about earnings quality, and it sensitizes you to the importance of this topic to your company, and to the integrity of the broader financial markets, then we will have achieved our objective.

John F. Morrow, CPA
AICPA Vice President
The New Finance

June 2001



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Comments on "Do the Right Thing"

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By Larry M. Prober, PhD, CPA

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differ. Examine the facts presented for County National Bank and determine the course of action you believe she should follow.

Comments on “Accounting for Loan Losses at County National Bank”

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By Larry M. Prober, Ph.D., CPA

Abstract

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Comments on “Accounting for In-Process R & D at Simpcos Incorporated”

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By Larry M. Prober, PhD, CPA

Abstract

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Comments on “Vision Technologies Incorporated”

Dan Hugo, CPA, is Director of External Reporting for EBay Inc.

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By Larry M. Prober, PhD, CPA

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Comments on “Restructuring at Exozol”

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By Larry M. Prober, PhD, CPA

Abstract

Jim Woods, controller of National Technology Corporation, a leading technology company, defends his company’s recent changes in pension plan assumptions as appropriate and realistic. Nevertheless, he realizes that pension plans are long-term commitments and that short-term economic conditions will always differ to some degree from the long-term assumptions selected. Thus, he has second thoughts about his company’s continuous attempts to adjust assumptions in calculating pension expense. His concerns are heightened by the impact of recent changes in the company’s reported income and the criticism of some members of the investment community. Read the following case facts and determine if criticisms of the company’s accounting are justified. Does Jim Woods have reason to be concerned?

Comments on “Accounting Issues at National Technology Corporation”

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By Lorri Carpenter, CPA

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Rising Star, an online discount retailer, has achieved success in a competitive market. To sustain that success, the company has made a series of strategic acquisitions. Now chief executive officer Jed Parker is faced with the possibility of accounting problems surrounding some of these deals—and the value of the deals themselves is even being called into question. Examine the facts presented for Rising Star and determine the course of action you believe Mr. Parker should follow.

Comments on “Is it Okay to Buy Earnings?”

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Comments on “A Troubled Acquisition for Websave”

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By Grace Morin, CPA

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Comments on “Accounting for a Windfall”

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Comments on “The Aker Computer Company”

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THE CASE OF BARTER TRANSACTIONS AND REVENUE RECOGNITION¹⁴⁴

By Chris Baker

Abstract

eCrawler.com is entering the home stretch on the road to its initial public offering. Dreams are soon to be realized. Two significant deals are closing that, taken together, should drive eCrawler through a successful public financing. But upon closer review in light of recent Securities and Exchange Commission and Emerging Issues Task Force barter revenue interpretations, the two defining agreements may not afford recognition of the anticipated revenue. Without the momentum generated from this revenue, the entire IPO could sink. What should eCrawler.com do? Examine the facts and determine the course of action you believe should be taken.

Comments on “The Case of Barter Transactions and Revenue Recognition”

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