

Contents at a Glance

<i>Introduction</i>	1
<i>Part I: Getting Down to Financial Reporting Basics</i>	7
Chapter 1: Opening the Cornucopia of Reports	9
Chapter 2: Recognizing Business Types and Their Tax Rules	21
Chapter 3: Public or Private: How Company Structure Affects the Books.....	29
Chapter 4: Digging into Accounting Basics	43
<i>Part II: Checking Out the Big Show: Annual Reports</i>	59
Chapter 5: Exploring the Anatomy of an Annual Report	61
Chapter 6: Balancing Assets against Liabilities and Equity	75
Chapter 7: Using the Income Statement.....	91
Chapter 8: The Statement of Cash Flows	107
Chapter 9: Scouring the Notes to the Financial Statements.....	121
Chapter 10: Considering Consolidated Financial Statements	139
<i>Part III: Analyzing the Numbers</i>	151
Chapter 11: Testing the Profits and Market Value.....	153
Chapter 12: Looking at Liquidity.....	171
Chapter 13: Making Sure the Company Has Cash to Carry On	181
<i>Part IV: Understanding How Companies Optimize Operations</i>	193
Chapter 14: How Reports Help with Basic Budgeting	195
Chapter 15: Turning Up Clues in Turnover and Assets	205
Chapter 16: Examining Cash Inflow and Outflow	217
Chapter 17: How Companies Keep the Cash Flowing.....	227

<i>Part V: The Many Ways Companies Answer to Others</i>	235
Chapter 18: Finding Out How Companies Find Errors: The Auditing Process.....	237
Chapter 19: Digging into Government Regulations	247
Chapter 20: Creating a Global Financial Reporting Standard.....	259
Chapter 21: Checking Out the Analyst-Corporation Connection.....	269
Chapter 22: How Companies Communicate with Shareholders	281
Chapter 23: Keeping Score When Companies Play Games with Numbers	295
<i>Part VI: The Part of Tens</i>	317
Chapter 24: Ten Financial Scandals That Rocked the World	319
Chapter 25: Ten Signs That a Company's in Trouble.....	329
<i>Glossary</i>	335
<i>Index</i>	343

<http://www.pbookshop.com>

Table of Contents

<i>Introduction</i>	1
About This Book	2
Conventions Used in This Book	2
What You're Not to Read	2
Foolish Assumptions	3
How This Book Is Organized	3
Part I: Getting Down to Financial Reporting Basics	4
Part II: Checking Out the Big Show: Annual Reports	4
Part III: Analyzing the Numbers	4
Part IV: Understanding How Companies Optimize Operations	4
Part V: The Many Ways Companies Answer to Others	5
Part VI: The Part of Tens	5
Icons Used in This Book	5
Where to Go from Here	6
<i>Part 1: Getting Down to Financial Reporting Basics</i>	7
Chapter 1: Opening the Cornucopia of Reports	9
Figuring Out Financial Reporting	9
Preparing the reports	10
Why financial reporting counts (and who's counting)	11
Checking Out Types of Reporting	12
Keeping everyone informed	13
Following the rules: Government requirements	14
Going global	15
Staying within the walls of the company: Internal reporting	15
Dissecting the Annual Report to Shareholders	17
Breaking down the parts	17
The meat of the matter	18
How the number crunchers are kept in line	19
Chapter 2: Recognizing Business Types and Their Tax Rules	21
Flying Solo: Sole Proprietorships	21
Keeping taxes personal	22
Reviewing requirements for reporting	22
Joining Forces: Partnerships	23
Partnering up on taxes	23
Meeting reporting requirements	24
Seeking Protection with Limited Liability Companies	24
Taking stock of taxes	24
Reviewing reporting requirements	25



Shielding Your Assets: S and C Corporations 25
 Paying taxes the corporate way..... 26
 Getting familiar with reporting requirements 27

Chapter 3: Public or Private: How Company Structure Affects the Books 29

Investigating Private Companies 29
 Checking out the benefits 30
 Defining disadvantages 31
 Figuring out reporting 32
Understanding Public Companies 33
 Examining the perks 35
 Looking at the negative side..... 35
 Filing and more filing: Government and shareholder reports 36
A Whole New World: How a Company Goes from Private to Public..... 39
 Teaming up with an investment banker 40
 Making a public offering..... 41

Chapter 4: Digging into Accounting Basics 43

Making Sense of Accounting Methods 43
 Cash-basis accounting..... 43
 Accrual accounting..... 44
 Why method matters..... 44
Understanding Debits and Credits 46
 Double-entry accounting..... 47
 Profit and loss statements 47
 The effect of debits and credits on sales 48
 Digging into depreciation and amortization..... 49
Checking Out the Chart of Accounts..... 50
 Asset accounts 51
 Liability accounts..... 53
 Equity accounts 54
 Revenue accounts..... 55
 Expense accounts 56
Differentiating Profit Types 57
 Gross profit 57
 Operating profit..... 58
 Net profit..... 58

Part II: Checking Out the Big Show: Annual Reports..... 59

Chapter 5: Exploring the Anatomy of an Annual Report 61

Everything but the Numbers 62
 Debunking the letter to shareholders 62
 Making sense of the corporate message..... 63
 Meeting the people in charge..... 64

Finding basic shareholder information.....	64
Getting the skinny from management	64
Bringing the auditors' answers to light.....	68
Presenting the Financial Picture.....	71
Summarizing the Financial Data	72
Finding the highlights.....	72
Reading the notes	73

Chapter 6: Balancing Assets against Liabilities and Equity 75

Understanding the Balance Equation	75
Introducing the Balance Sheet.....	76
Digging into dates	76
Nailing down the numbers.....	78
Figuring out format.....	78
Ogling Assets.....	80
Current assets	80
Long-term assets.....	83
Accumulated depreciation	86
Looking at Liabilities	87
Current liabilities	87
Long-term liabilities.....	88
Navigating the Equity Maze.....	89
Stock.....	89
Retained earnings.....	90
Capital	90
Drawing	90

Chapter 7: Using the Income Statement. 91

Introducing the Income Statement.....	92
Digging into dates	93
Figuring out format.....	93
Delving into the Tricky Business of Revenues.....	96
Defining revenue	96
Adjusting sales	97
Considering cost of goods sold.....	99
Gauging gross profit	100
Acknowledging Expenses	101
Sorting Out the Profit and Loss Types.....	103
EBITDA	103
Nonoperating income or expense.....	104
Net profit or loss	105
Calculating Earnings per Share.....	105

Chapter 8: The Statement of Cash Flows 107

Digging into the Statement of Cash Flows	107
The parts.....	108
The formats	109

Checking Out Operating Activities	111
Depreciation	111
Inventory.....	112
Accounts receivable.....	112
Accounts payable	113
Summing up the cash-flow-from-activities section.....	113
Investigating Investing Activities.....	114
Understanding Financing Activities	115
Issuing stock.....	115
Buying back stock.....	115
Paying dividends.....	116
Incurring new debt	116
Paying off debt	117
Recognizing the Special Line Items	117
Discontinued operations.....	117
Foreign currency exchange	118
Adding It All Up.....	118

Chapter 9: Scouring the Notes to the Financial Statements 121

Deciphering the Small Print	122
Accounting Policies Note: Laying Out the Rules of the Road	122
Depreciation	123
Revenue.....	124
Expenses	124
Figuring Out Financial Borrowings and Other Commitments.....	126
Long-term obligations	126
Short-term debt.....	129
Lease obligations	130
Mergers and Acquisitions: Noteworthy Information	131
Pondering Pension and Retirement Benefits	132
Breaking Down Business Breakdowns.....	133
Reviewing Significant Events.....	135
Finding the Red Flags	136
Finding out about valuing assets and liabilities.....	137
Considering changes in accounting policies.....	137
Decoding obligations to retirees and future retirees.....	138

Chapter 10: Considering Consolidated Financial Statements 139

Getting a Grip on Consolidation	139
Looking at Methods of Buying Up Companies.....	144
Reading Consolidated Financial Statements.....	146
Looking to the Notes	148
Mergers and acquisitions	149
Goodwill	149
Liquidations or discontinued operations	150

***Part III: Analyzing the Numbers*..... 151**

Chapter 11: Testing the Profits and Market Value153

The Price/Earnings Ratio..... 154
 Figuring out earnings per share..... 154
 Calculating the P/E ratio 155
 Practicing the P/E ratio calculation..... 156
 Using the P/E ratio to judge company
 market value (stock price)..... 157
 Understanding variation among ratios 159
 The Dividend Payout Ratio..... 160
 Determining dividend payout..... 160
 Digging into companies' profits with dividends 161
 Return on Sales 163
 Figuring out ROS 163
 Reaching the truth about profits with ROS 164
 Return on Assets..... 164
 Doing some dividing to get ROA 165
 Ranking companies with the help of ROA 165
 Return on Equity..... 165
 Calculating ROE..... 166
 Reacting to companies with ROEs assistance..... 166
 The Big Three: Margins..... 167
 Dissecting gross margin..... 167
 Investigating operating margin 168
 Catching the leftover money: Net profit margin 169

Chapter 12: Looking at Liquidity171

Finding the Current Ratio 172
 Calculating the current ratio 172
 What do the numbers mean? 173
 Determining the Quick Ratio..... 173
 Calculating the quick ratio..... 173
 What do the numbers mean? 174
 Investigating the Interest Coverage Ratio 175
 Calculating the interest coverage ratio..... 175
 What do the numbers mean? 176
 Comparing Debt to Shareholders' Equity..... 176
 Calculating debt to shareholders' equity 177
 What do the numbers mean? 178
 Determining Debt-to-Capital Ratio 178
 Calculating the debt-to-capital ratio..... 178
 What do the numbers mean? 180

Chapter 13: Making Sure the Company Has Cash to Carry On181

Measuring Income Success	181
Calculating free cash flow	182
Figuring out cash return on sales ratio.....	184
Checking Out Debt.....	185
Determining current cash debt coverage ratio.....	186
Computing cash debt coverage ratio	188
Calculating Cash Flow Coverage.....	190
Finding out the cash flow coverage ratio.....	190
Hasbro	192
What do the numbers mean?	192

Part IV: Understanding How Companies Optimize Operations 193**Chapter 14: How Reports Help with Basic Budgeting.....195**

Peering into the Budgeting Process	196
Who does what.....	196
Setting goals	197
Building Budgets.....	199
Providing Monthly Budget Reports.....	201
Using Internal Reports	203

Chapter 15: Turning Up Clues in Turnover and Assets205

Exploring Inventory Valuation Methods.....	206
Applying Three Inventory Valuation Methods	208
Average costing.....	209
FIFO.....	210
LIFO.....	210
Comparing inventory methods and financial statements	211
Determining Inventory Turnover	211
Calculating inventory turnover.....	212
What do the numbers mean?	213
Investigating Fixed Assets Turnover.....	214
Calculating fixed assets turnover	214
What do the numbers mean?	215
Tracking Total Asset Turnover.....	215
Calculating total asset turnover.....	215
What do the numbers mean?	216

Chapter 16: Examining Cash Inflow and Outflow217

Assessing Accounts Receivable Turnover	217
Calculating accounts receivable turnover.....	218
What do the numbers mean?	219

Taking a Close Look at Customer Accounts 220

Finding the Accounts Payable Ratio 222

 Calculating the ratio 222

 What do the numbers mean? 223

Determining the Number of Days in Accounts Payable..... 223

 Calculating the ratio 223

 What do the numbers mean? 224

Deciding Whether Discount Offers Make Good Financial Sense 225

 Calculating the annual interest rate 225

 What do the numbers mean? 226

Chapter 17: How Companies Keep the Cash Flowing 227

 Slowing Down Bill Payments 227

 Speeding Up Collecting Accounts Receivables..... 228

 Borrowing on Receivables..... 230

 Reducing Inventory 231

 Getting Cash More Quickly..... 232

Part V: The Many Ways Companies Answer to Others 235

Chapter 18: Finding Out How Companies Find Errors: The Auditing Process 237

 Inspecting Audits and Auditors 237

 Looking for mistakes 238

 Meeting Mr. or Ms. Auditor 238

 Examining Records: The Role of the Auditor..... 239

 Preliminary review..... 240

 Fieldwork 240

 Audit report 242

 Filling the GAAP 242

 Accounting standards: Four important qualities..... 243

 Changing principles: More work for the FASB 244

Chapter 19: Digging into Government Regulations 247

 Checking Out the 10-Q 248

 Financial information 248

 Other critical matters..... 249

 Introducing the 10-K..... 250

 Business operations 250

 Financial data 250

 Information about directors and executives 252

 The extras 252

 Investigating Internal Controls 253

Uncovering the Ways Companies Keep in Compliance.....	254
Digging into Board Operations	256
The nominating process	256
Contacting board members.....	257
Finding Out about Insider Ownership.....	258
Chapter 20: Creating a Global Financial Reporting Standard	259
Why Develop a Worldwide Financial Standard?.....	259
Key Moves to Reshape Global Financial Reporting	260
Who Benefits from a Global Standard and How?.....	261
Investors	261
Capital Markets	262
Companies	262
Exploring Key Differences between GAAP and IFRS	262
Accounting framework.....	263
Financial statements.....	263
Revenue recognition.....	265
Assets	265
Inventory.....	266
Related-party transactions-disclosures	266
Discontinued operations.....	267
Impairment charges.....	267
Chapter 21: Checking Out the Analyst-Corporation Connection . . .	269
Typercasting the Analysts	269
Buy-side analysts	270
Sell-side analysts.....	271
Independent analysts	273
Bond analysts.....	274
Regarding Bond Rating Agencies.....	274
Delving into Stock Rating.....	276
Taking a Look at How Companies Talk to Analysts	277
Analyst calls.....	277
Press releases.....	278
Road shows.....	279
Chapter 22: How Companies Communicate with Shareholders . . .	281
Making the Most of Meetings	282
Checking Out How the Board Runs the Company.....	283
Watching the directors	283
Speaking out at meetings	284
Moving away from duking it out	285
Sorting through Reports	286
Catching Up on Corporate Actions	287
Culling Information from Analyst Calls.....	288
Listening between the lines.....	289
Knowing when to expect analyst calls	292

Staying Up to Date Using Company Web Sites.....	292
Regarding Reinvestment Plans	293
Dividend-reinvestment plans	293
Direct-stock-purchase plans.....	294

Chapter 23: Keeping Score When Companies

Play Games with Numbers 295

Getting to the Bottom of Creative Accounting	296
Defining the scope of the problem	296
Recipes for cooked books.....	297
Unearthing the Games Played with Earnings.....	298
Reading between the revenue lines.....	299
Detecting creative revenue accounting	303
Exploring Exploitations of Expenses.....	305
Advertising expenses	306
Research and development costs.....	306
Patents and licenses.....	307
Asset impairment.....	308
Restructuring charges.....	309
Finding Funny Business in Assets and Liabilities.....	309
Recognizing overstated assets.....	310
Looking for undervalued liabilities.....	312
Playing Detective with Cash Flow.....	314
Discontinued operations.....	314
Income taxes paid.....	315

Part VI: The Part of Tens..... 317

Chapter 24: Ten Financial Scandals That Rocked the World. 319

Enron.....	320
Citigroup.....	321
Adelphia.....	321
WorldCom/MCI	322
Sunbeam	323
Tyco.....	323
Waste Management	324
Bristol-Meyers Squibb.....	325
Halliburton	325
Arthur Andersen.....	326

Chapter 25: Ten Signs That a Company's in Trouble 329

Lower Liquidity.....	329
Low Cash Flow	330
Disappearing Profit Margins.....	330
Revenue Game-Playing.....	331

Too Much Debt	332
Unrealistic Values for Assets and Liabilities.....	332
A Change in Accounting Methods	332
Questionable Mergers and Acquisitions	333
Slow Inventory Turnover.....	334
Slow-Paying Customers.....	334
<i>Glossary</i>	335
<i>Index</i>	343

<http://www.pbookshop.com>