Steve Wiggs Case Scenario

Steve Wiggs, CFA, is an analyst at Wickerman Investments. He is analyzing the financial statements of a company, Texas Ryders. The company has acquired a stake of 80% in Nozil Corporation. Texas Ryders had paid $560 million for the stake. The abridged balance sheet of Nozil Corporation just before the acquisition is given in Exhibit 1.

Exhibit 1
Nozil Corporation (in millions of US dollars)

Current Assets	310
Noncurrent assets	750
Goodwill	80
Current Liabilities	120
Noncurrent liabilities	420
Stockholders' equity	600

Both companies, Texas Ryders and Nozil Corporation, are following U.S. GAAP for reporting purpose. All the values in Exhibit 1 are book values. The fair value of noncurrent assets is $150 million more than the book value.

Steve Wiggs converts the financial statements of Texas Ryders according to IFRS as he has to compare it with the other companies following IFRS.

Steve also finds out that in the recent financial statement, Texas Ryders has reported the impairment losses. He checks the recent financial statements of Nozil Corporation and extracts out the important information which is presented in Exhibit 2.

Exhibit 2
Nozil Corporation (in millions of US dollars)

Fair value of equity	540
Fair value of net assets	520

Ryan Herbert, another analyst at the same firm, asks Steve about the impact of using different approaches of reporting goodwill on the financial ratios and other financial entries. Steve Wiggs makes the following statements:

Statement 1: Under full goodwill approach, the minority interest is lower as compared to the partial goodwill approach
Statement 2: Under full goodwill approach, the asset turnover ratio is lower as compared to the partial goodwill approach
Statement 3: Under partial goodwill approach, the return on equity is higher as compared to the full goodwill approach

Ryan Herbert says that there are three methods by which companies can report the acquisition of other company on their balance sheet. The three methods are proportionate consolidation method, equity method, and acquisition method. He asks Steve two questions.

Question 1: What is the return on equity using proportionate consolidation method as compared to other two methods?
Question 2: Which of the methods leads to the highest net income?

1. What is the amount of goodwill Texas Ryders should report as goodwill in its consolidated balance sheet on acquiring the stake of Nozil Corporation if it follows full goodwill approach?
   a) $30 million
   b) $60 million
   c) $180 million

2. What is the amount of goodwill reported in the consolidated balance sheet of Texas Ryders if it follows partial goodwill approach?
   a) $24 million
   b) $60 million
   c) $144 million

3. Which of the following statements made by Steve Wiggs regarding the comparison of full goodwill approach and partial goodwill approach is least likely to be correct?
   a) Statement 3
   b) Statement 2
   c) Statement 1

4. What is the total impairment of goodwill reported by Nozil Corporation on its balance sheet?
   a) $4 million
   b) $10 million
   c) $20 million

5. What is the answer to Question 1 asked by Ryan Herbert?
   a) Greater than equity method and lesser than acquisition method
   b) Same as equity method and greater than acquisition method
   c) Lesser than equity method and greater than acquisition method

6. What is the answer to Question 2 asked by Ryan Herbert?
   a) Equity method
   b) Acquisition method
   c) All three methods yield the same net income

Greg Prine Case Scenario

Greg Prine, CFA, is discussing the impact of currency translation methods on various financial statement items with his colleague Sir Ravindra Jadeja, CFA FRM CAIA PHD MBA CFP. The parent's presentation currency is USD and the foreign currency is EUR.

Greg Prine: If the exchange rate changes from 1.2 USD/EUR to 1.22 USD/EUR, then the liabilities of the subsidiary company after currency translation will increase if there is net monetary asset exposure under temporal method. Under current rate method, the liabilities will increase.

Sir Ravindra Jadeja: If the exchange rate changes from 1.2 USD/EUR to 1.18 USD/EUR, then there will be a net translational loss for the subsidiary if there is net monetary liability exposure under temporal method. Under current rate method, there will be a negative translational adjustment in the balance sheet.

Greg Prine: If the exchange rate changes from 1.2 USD/EUR to 1.18 USD/EUR, then the shareholders' equity of the subsidiary after currency translation will decrease in case of net monetary asset exposure under temporal method. Under current rate method, the shareholders' equity will decrease.

Sir Ravindra Jadeja: If the exchange rate changes from 1.2 USD/EUR to 1.22 USD/EUR, then the net income after translation for subsidiary will increase in case there is net monetary liability exposure under temporal method. Under current rate method, the net income will increase.

Greg Prine: If the exchange rate changes from 1.2 USD/EUR to 1.22 USD/EUR, then the total profit after translation adjustment for the subsidiary will be more than if the currency exchange rate would have changed from 1.2 USD to 1.21 USD/EUR under temporal rate method.

Sir Ravindra Jadeja: If the subsidiary functional currency is facing hyperinflation and they have a land on its balance sheet, the translated amount of the land will be more than the historical amount in case the exchange rate has changed by 80% in last 3 years and the total cumulative inflation has been 120%. The parent is following the translation method under IAS 21 where the financial statement entries are restated for inflation and then translated using the current exchange rate.

7. Are the statements made by Greg Prine correct regarding the change in liabilities after currency translation for the subsidiary?
   a) Incorrect for temporal method and correct for current rate method
   b) Correct for both the methods
   c) Incorrect for both the methods

8. Are the statements made by Sir Ravindra Jadeja correct regarding the translational loss and translational adjustments after currency translation?
   a) Correct for both the methods
   b) Correct for temporal method and incorrect for current rate method
   c) Incorrect for temporal method and correct for current rate method

9. Are the statements made by Greg Prine correct regarding the change in shareholders' equity after currency translation?
   a) Correct for both the methods
   b) Incorrect for temporal method and correct for current rate method
   c) Correct for temporal method and incorrect for current rate method

10. Are the statements made by Sir Ravindra Jadeja correct regarding the change in net income after currency translation?
   a) Correct for both the methods
   b) Correct for temporal method and incorrect for current rate method
   c) Incorrect for temporal method and correct for current rate method

11. Is the statement made by Greg Prine correct for the change in total profit after the currency translation for different exchange rates?
   a) Yes
   b) No
   c) Can't say

12. Is the statement made by Sir Ravindra Jadeja correct about the impact on the value of asset under hyperinflation after currency translation for the stated method?
   a) Yes
   b) No
   c) Can't say

Will Brown Case Scenario

Will Brown is an accountant in Vickery Inc. His primary job is to prepare annual financial statements for the company which can be presented to the stakeholders. Vickery Inc. is a US based company and it has a 100% owned subsidiary in Greece. The subsidiary is Mickey Inc. It started its operations at the beginning of 2012. The functional currency of Mickey Inc. is USD and it has to present its financial statements in Euro. The presentation and functional currency of Vickery Inc. is USD. The income statement and balance sheet for Mickey Inc. for year ending 2012 are given in Exhibit 1.

Exhibit 1
Balance Sheet (in thousands of Euros)

As of 31 December	**2012**
Cash and cash equivalents	320
Accounts receivable	280
Inventories	450
Total Current Assets	1,050
Property, plant and equipment	1,950
Less: accumulated depreciation	100
Total assets	**2,900**
Accounts payables	250
Total current liabilities	250
Long-term debt	1,480
Total liabilities	1,730
Common stock and paid in capital	1,020
Retained earnings	150
Total shareholders’ equity	1,170
Total liabilities and shareholders’ equity	**2,900**

Income Statement and Statement of Retained Earnings (in thousands of Euro)

For the year ended 31 December	**2012**
Sales	1,800
Cost of goods sold	750
Depreciation and amortization expense	100
SG&A	350
Interest expense	150
Income tax expense	180
Net income	270
Less: Dividends, 15 Nov 2012	120
Retained earnings, 31 December 2012	150

The company also reports the following information in its notes to financial statements:
The inventory is measured at historical cost on a FIFO basis.
Brown gathers the information about the exchange rates throughout the year to translate the financial statements of Mickey Inc. into USD. The information is provided into Exhibit 2.

Exhibit 2
Exchange rates

Date	USD per Euro
1 January 2012	1.18
Average, 2012	1.22
Weighted average rate when inventory was acquired	1.20
15 November 2012 when dividends were declared	1.23
31 December 2012	1.24

13. What is the total retained earnings for Mickey Inc. after currency translation to USD in 2012?
   a) $118,200
   b) $183,000
   c) $200,800

14. What is the net income for Mickey Inc. after currency translation to USD in 2012?
   a) $265,800
   b) $112,400
   c) $93,400

15. What is the value of total current assets for Mickey Inc. after currency translation at the end of 2012?
   a) $1,302,000
   b) $1,284,000
   c) $1,272,800

16. What is the value of total liabilities for Mickey Inc. after currency translation at the end of 2012?
   a) $2,145,200
   b) $2,115,600
   c) $2,056,400

17. What is the value of fixed asset turnover for Mickey Inc. after currency translation for the year 2012?
   a) 0.954
   b) 1.006
   c) 1.040

18. What is the value of operating profit margin for Mickey Inc. after currency translation for the year 2012?
   a) 25.86%
   b) 27.40%
   c) 34.20%

Robert Paulson Case Scenario

Robert Paulson is a CFA level II candidate. He is analyzing the financial statement of MTR Inc. MTR Inc. had given share based compensation to their employees. The company had granted shares to its employees in 2009. The total shares granted were 2 million. The granted shares were based on the vesting period. The cost of the share based expense was recognized over a weighted average period of 2.5 years. The additional details can be found in Exhibit 1.

Exhibit 1

Grant date	1st July 2009
Weighted average vesting period date	1st January 2012
Share price on 1st July 2009	$15.40
Share price on 1st January 2011	$16.80
Share price on 1st January 2012	$18.00
Weighted average share price in 2010	$16.20
Weighted average share price in 2011	$17.45

The company further granted 50,000 shares on 1 January 2011 which were vested immediately.

MTR Inc. has provided the following disclosures in the financial statements of the company:

Disclosure 1: How the stocks will be granted to the employees and what are the requirements to be fulfilled by the employees to get those shares.
Disclosure 2: The effect of share based compensation on the company's reported income for the year
Disclosure 3: How the fair value of share based compensation has been determined
Disclosure 4: The impact of share-based compensation on the cost of capital of the company
Disclosure 5: The impact of share based compensation on the financial position of the company

Bob Cornelius, colleague of Robert Paulson, asks him to explain the share-based compensation used by the firms. Robert Paulson makes the following statements:

Statement 1: The two common forms of equity-settled share based compensation are stock grants and stock options. Stock appreciation rights or phantom stocks are other form of share based compensation.
Statement 2: Under US GAAP and IFRS, the expense related to the stock grants is always expensed in the period in which the shares are granted. The expense is calculated as the fair value of shares granted.
Statement 3: Under US GAAP and IFRS, the expense related to stock options is expensed over the period between the grant date and exercise date. The expense is calculated as the fair value of options.
Statement 4: The fair value of options is equal to the market value of options at the grant date.

Bob Cornelius further asks the following questions:
Question 1: Which of the share based compensation methods leads to a cash outflow in the current period and which one doesn't lead to dilution of shareholder ownership?
Question 2: In which of the share based compensation methods, there is most potential of risk aversion?

19. What is the approximate compensation expense related to the shares granted for the firm in 2009?
   a) $6.16 million
   b) $12.32 million
   c) $30.8 million

20. What is the approximate share based compensation expense reported by the firm in 2011?
   a) $0.84 million
   b) $13.16 million
   c) $14.80 million

21. Which of the following disclosures is/are least likely to be required under US GAAP?
   a) Disclosure 3 and Disclosure 5
   b) Disclosure 4 and Disclosure 5
   c) Disclosure 4 only

22. Which of the following statements made by Robert Paulson is/are least likely to be accurate?
   a) Statement 2 and Statement 4
   b) Statement 2 and Statement 3
   c) Statement 2, Statement 3, and Statement 4

23. What is the answer to Question 1 by Bob Cornelius?
   a) Cash outflow for stock grants and no dilution under stock appreciation rights
   b) Cash outflow for stock appreciation rights and no dilution for stock options
   c) Cash outflow and no dilution under stock appreciation rights

24. What is the answer to Question 2 by Bob Cornelius?
   a) Stock grants
   b) Stock options
   c) Stock appreciation rights

Scott Thomas Case Scenario

Scott Thomas is analyzing the financial statements of Scotch & Scotch Inc. The company is following the defined benefit plan for its employees. He extracted the details from the financial statements and those details have been provided in Exhibit 1.

Exhibit 1 (in million of USD)

Year	2011	2012
Planned assets at the beginning of year	674	-
Contribution made at the end of year	120	38
Actual return on planned assets	62	84
Current service cost	75	80
Projected benefit obligation at the beginning of year	712	-
Actuarial gain due to changes in actuarial assumptions	(26)	42
Accumulated unamortized past service costs	124	-
Accumulated unamortized total actuarial gain	(72)	-

The expected return on planned assets is 11% and the yield on high quality corporate bonds for the company is 9.5%. The company is following U.S. GAAP for its reporting purposes. The average service lives of employees are assumed to be 10 years over which the costs would be amortized. The average service lives is assumed to be remain constant considering the firm to be on going on concern basis.

The company is following the corridor approach to recognize actuarial gains or losses. If the cumulative amount of unrecognized net gain or loss exceeds 10% of the greater of the value of the planned assets or the projected benefit obligation, the difference is amortized over the service lives of the employees. The company has not paid any benefits to employees during these years.

Novak Johnson, a friend of Scott Thomas, asks him about the impact of the change in assumptions on the net pension obligation. Scott makes the following statements:

Statement 1: The increase in the assumed discount rate decreases the pension obligation.

Statement 2: The increase in the assumed annual compensation growth rate decreases the pension obligation.

Statement 3: The increase in the assumed discount rate increase the interest cost of current period.

He further asks the impact of increase in expected return on plan assets on the periodic pension cost under U.S. GAAP.

25. What is the total change in P&L in 2011 due to the defined benefit compensation plan only?
a) Loss of $94.5 million
b) Loss of $106.64 million
c) Loss of $126.24 million

26. What is the total change in OCI in 2011 due to the defined benefit compensation plan only?
a) Decrease by $48.04 million
b) Decrease by $67.64 million
c) Decrease by $86.18 million

27. What is the value of planned assets at the beginnings of year 2013? Ignore taxes in your calculations.
a) $820 million
b) $978 million
c) $1,001.64 million

28. What is the funded status of company in 2011?
a) Net liability of $24.64 million
b) Net liability of $50.64 million
c) Net liability of $144.64 million

29. Which of the following statements made by Scott Thomas is least accurate?
a) Statement 1
b) Statement 2
c) Statement 3

30. What is the impact of increase in expected returns on the periodic pension expense under U.S. GAAP?
a) Decrease in periodic pension expense
b) No change in periodic pension expense
c) Increase in periodic pension expense