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Beyond Problems and Cases: Discussion Materials for Accounting in Executive Programs

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Abstract

Selection or development of classroom materials for an accounting class in an executive program is complicated by the fact that some students enter the program with a substantial knowledge of accounting while others may have no background at all. Furthermore, general management programs do not usually focus on making all students equally knowledgeable about what accountants do and how to use the information that accounting provides. Problems and cases are sometimes not successful as discussion materials in the mixed audience class because some students are not challenged while others are overwhelmed because of their lack of exposure to the methods and principles of accounting. We describe a new class of materials prepared for executive program accounting classes that are based on contemporary events that become the bases for informed discussion among students where learning takes place at each student's level while working in small groups to understand the problems, possible solutions, and actions that might be taken to clarify issues and solutions to the problems posed. Three examples are described and illustrated.

Introduction

Teaching financial accounting in an Executive MBA or company sponsored program for managers with diverse backgrounds presents some significant challenges. Some of these include great differences in knowledge and experience with accounting, unexpressed fears about a subject perceived as highly technical, and many fears about being exposed as unknowledgeable about a core area of critical business background. Problems and case studies are one way to deal with these challenges, but it is difficult to find simple problems and cases that help the least prepared students to learn while challenging the most expert to improve their own knowledge at the same time. We will explore the development and use of discussion materials based on contemporary financial reports and situations that allow groups of diverse managers to all learn more about accounting in the same groups and classrooms. We will focus attention on Executive MBA programs (EMBA), but the discussion materials we will present are also applicable to many other executive programs and even some undergraduate courses.

Goals for our Accounting Course in an EMBA Program

No one enrolls in an EMBA program to become an accountant. In fact, many of our EMBA students have told us that they would just as soon skip the study of accounting and get on to the study of other subjects like marketing, manufacturing, management, and finance. The fears that many of our executive students have of accounting often border on irrationality. Many of them got where they are because they were excellent students in arts and sciences who were hired by companies just looking for good people. Some were music majors, graphic design majors, or engineers, who now find themselves in managerial positions that require new knowledge and skills. They often believe that everyone else is an expert in accounting and finance, and they have been faking understanding of those subjects as they have assumed new responsibilities, nodding agreement and pretending to understand in meetings and at financial presentations. Other instructors from other programs have told us, and we have observed in company-sponsored executive development programs, that students who are enrolled in those programs who did not previously study accounting arrive with a feeling of fear and inferiority.

The EMBA accounting instructor has to do several things to alleviate these fears. Being explicit about goals is a first step, and we use three goals to help the choice of materials and classroom style.

Learn to speak conversational accounting. Accounting is often called the “language of business,” and we need to learn vocabulary and syntax to speak about accounting matters. Accounting is the language that we often use in organizations to talk to other functional areas. It is the language that we must use to ask for information we need that is in the hands and minds of other areas. Managers need to understand the financial reporting ramifications of decisions that they and their colleagues are contemplating or making.

Improve financial analysis skills. Managers need to know how accounting systems measure assets, liabilities, revenues, and expenses, and how they produce financial statements and other reports. They need to understand how accounting choices, estimates, and rules affect financial statements and the quality of information that is available within an organization. Understanding what accounting does well and what it does poorly helps students to develop comparative analysis and ratio skills.

Recognize and be aware of ethical issues in accounting. Examples of financial scandals should be used to sharpen understanding of problem areas. The use of estimates and pitfalls in the processes accounting uses to recognize revenues and expenses need to be revealed and explored. The designs and processes used by institutions charged with addressing ethical issues in accounting need to be revealed and discussed by students about to assume greater executive responsibilities.

These goals cannot be met by assigning problems with presumed answers or cases that are problems in disguise. Discussion materials that emphasize current issues that are relevant to executive students in their present jobs and in the current economy are needed. Furthermore, these should be selected to exploit the diversity of background training and experiences that we expect to find in the EMBA classroom. The classroom discussions should build seamlessly on what executive students are experiencing in their jobs and reading in the business and financial press reports.

Before our discussion materials are used, students need some basic knowledge of accounting and the structure of financial statements. We address this in several ways early in the program. First, we send a programmed learning textbook such as Anthony’s *Essentials of Accounting* or a computer based learning CD as a preprogram assignment before our first class so that everyone has some common vocabulary and ideas about

how an accounting system works. Our program starts with a week-long residency at a conference center owned by the university. Within this residency, there are two long introductory accounting sessions that are used to take the students through the preparation of the major financial statements, including the use of journal entries to follow transactions. We want to assure that everyone knows the basic rules of bookkeeping and how financial statements such as balance sheets, income statements, and statements of cash flows are prepared.

In the past we have used some form of annual report project to teach financial analysis and relate accounting techniques to real companies in our EMBA program. We have also asked students to keep a journal relating current curriculum topics to their own job and company. While both of these techniques have been successful to some degree, but we have found a third technique that seems to truly enhance the class experience once the basic accounting techniques have been introduced.

In-Class Company Exercises

In each EMBA program we try to use three in-class current financial analyses as group exercises. Our EMBA classes are close to three hours long, and these little projects provide a welcome, but educational break that usually takes between 45 minutes and an hour, including groups breaking out to work on the exercises, then returning to the classroom for discussion. Our assignments and materials must meet four criteria.

1. Materials must be from contemporary sources (newspapers, magazines, or internet reports), preferably almost real time sources.
2. There must be enough complexity in the exercise to enable those with prior skills to suggest techniques for analysis that will enhance the knowledge of others in the group.
3. The companies should have some interesting issues that will further learning.
4. The material should not be overwhelming in complexity or magnitude.

Our experiences with these group exercises have evolved over the years. Some of our best materials have been very time-consuming for the professor, given the need to research and essentially prepare a classroom

exercise with a few days. However, we have found that it is possible to prepare a successful educational exercise with a minimal expenditure of effort by starting simply.

Exercise 1: The Good, the Bad, and the Interesting

It is amazing how much insight and discussion you can generate by a simple instructional page asking the groups to identify (1) three bad signs; (2) three good signs; and (3) three interesting issues for which they need more information, accompanied by basic financial statements and a recent stock chart. Exhibit 1 illustrates how you can present a very simple exercise using these basic questions, perhaps supplemented by some directional questions. Our financial course begins in January, which means that most companies' annual filings with the SEC will be from the previous spring. This has caused us to need to provide more recent financial information, and some business internet sites like CNN Money and Yahoo Finance are good sources for summarized quarterly data. This also serves as a learning device, with students trying to discern how to use the quarterly data. Good sources for stock charts include BigCharts.com and StockCharts.com.

Today's technology makes it possible to find a large number of instant analyses of any company, and since our students bring laptops to classrooms with wireless connectivity, we have found that removing identifying information such as company name, stock ticker symbol, etc. leads to a better learning experience. This usually means they will work on the unidentified company data first, before reaching the "what company do you think this is?" question that forces them to search for their own data in real time during the class. At this point, students are very resourceful in figuring out the company. It is also helpful to make sure a few clues to the nature of the business are included in the exercise. Using interesting companies in the news is the key to a successful experience. For example, we used the "Good, Bad, and Interesting" format during the Iraq war using Halliburton and during the gas price run-up using SunPower, a solar panel company. The first exercise of 2010 used American Science and Engineering (AS&E), a major manufacturer of full-body scanners, from an industry affected by the recent Christmas Day airline event. That example included slightly reworded risk factors from the company's 10-k that hinted that something had affected the company's stock price shortly after Christmas. The instructional page and Risk Factor Exhibit from AS&E are presented in Exhibit 2.

Exercise 2: Quick Opportunities from News Events

We keep a close watch on the business pages during EMBA classes, but sometimes just the general news of the day provides an opportunity for a current exercise. This happened on February 9, 2010, when WellPoint raised some of its health premium rates in California by 39 percent in the midst of debate on the health care bill. We used this event for an exercise three days later, partially to exploit the chance to be incredibly relevant and up-to-date, but also to give the groups an opportunity to look at a specific industry that looks a little different from your basic manufacturing industry. Given the nature of the story, the company was not disguised and students were encouraged to use the internet for research. Instructions for the case are presented as Exhibit 3. With this case, as with the Halliburton case, it was important to avoid bringing our personal political point of view into the case and to try to remain neutral during the discussion.

Exercise 3: Company Comparisons

This year we used an anonymous comparison of two major players in one industry very successfully. The financial pages had alerted us to a legal battle going on between United Parcel Service (UPS) and Federal Express (FedEx) concerning whether drivers were employees or independent contractors. When you double the amount of information to be analyzed, it can be overwhelming for a short exercise, so we made the questions very directive and included columns on the income statement showing accounts as a percentage of sales and on the balance sheet, accounts as a percent of total assets. About this time, our EMBA administration was encouraging us to make sure the students realized the important connections between the classes. As the students were also taking marketing and economics, we included an integration question in the exercise, which worked very well in comparing the companies' financial results in relation to their marketing strategies and how they function in their regulatory environment. The UPS/FedEx exercise instructions, risk factors and common sized financial statements are presented in Exhibit 4.

The Payoffs for EMBA Students and Course Instructors

Students love the substitution of timely and relevant course material to replace textbook problems and cases from the past. Utilizing the knowledge and skill of knowledgeable peers to teach the beginners in the program gives status to the former while helping everyone to enter into the discussion of issues, methods, and conclusions. Financial analysis skills are improved for everyone whether expert or beginner. In our long class periods we can begin with some commentary and illustrations and then use one of the current issues for a thirty to forty-five minute small group discussion before coming back into class mode for a summary discussion by the entire class. Groups do different things and draw different conclusions which always lead to vigorous debate and discussion. We always try to end this discussion by asking the class what they had learned from the exercise and summarizing these learnings on the boards in the classroom.

At the course midpoint and end, we use examinations that also have enough latitude and ambiguity that the best students can use their deeper knowledge to show their superior analyses and solutions, while other students can show that they have learned more than just rules, conventions, and statement formats. We also use questions that we have not discussed in class, but which draw on a student's abilities to apply the same thinking processes that groups have used during our in class discussions. We plan to use materials like those that we have been discussing in class in future exams, but to date we have not done so. Course evaluations and grades are assigned based on the quality of thinking revealed and the ingenuity shown in commenting and writing shown in exams and class participation.

The final payoffs are for the instructor. Students know that their instructor is up to date and is living in his or her subject. The knowledge is current and relevant for students in their jobs and lives. Accounting becomes fun and relevant, and that makes the teaching fun and rewarding.

Exhibit 1

Easy to Prepare Group Exercises

BASIC GROUP EXERCISE

1. Scan the data on the following pages. These data include (1) annual income statements, balance sheets, and cash flow statements through Dec. 20XX; (2) quarterly data for 20XX through Sept; and (3) stock price and volumes for 20XX.
2. Come back to class with at least three “good” things you see, three “bad” things you see, and three questions that you would want answered before investing in this company.

SAMPLE ADDITIONAL DIRECTIVE QUESTIONS

1. Is the company small, medium, large, or extra-large? What measures might you use to address size?
2. Is it a manufacturing, retail, or service company or hybrid?
3. How liquid are the company’s assets?
4. What does their financial structure look like?
5. What are the major sources of their cash flows?
6. What do trends in assets, sales, income, taxes, and stock price tell you about the company?

Exhibit 2

EMBA Group Exercise – Friday, January 15, 2010

(This was American Science and Engineering)

(Financial statements and stock charts are not included in this exhibit.)

The following pages present information on an unidentified company. Break into your groups for 30 minutes and complete the following tasks.

1. Familiarize yourself with what is presented:
 - a. Exhibit 1: Selected *Business Risk Factors* from the company’s Annual Report and 10-K (SEC filing).

- b. Exhibit 2: 15 month stock chart and 3 month stock chart
 - c. Exhibit 3: An income statement with March 31, 2009 fiscal year end and quarterly income statements for July 30 and September 30, 2009.
 - d. Exhibit 4: A balance sheet with March 31, 2009 fiscal year end.
 - e. Exhibit 5: A cash flow statement with a March 31, 2009 fiscal year end.
2. Answer the following specific questions:
- a. Is this a large, medium, or small company?
 - b. Calculate the gross margin % for 2007, 2008, and 2009 separately for product sales and service revenue. What does this tell you about 2008 income?
 - c. What is the trend in research and development expenditures?
 - d. How does the stock price activity compare to what you know about stock market trends during 2009? What happened to the stock price and volume starting on December 28, 2009?
 - e. What percentage of total assets are (1) cash; (2) inventories; (3) property, plant and equipment? What does this tell you about the liquidity and asset structure of the company?
 - f. What are the major current liabilities? What does that tell you about the nature of their business and customers?
 - g. What are the major investing uses of cash? Financing uses of cash?
 - h. From the Risk Factors and other data, can you guess what industry and/or company this is?
3. In general, come back to class ready to talk about the good, bad, or interesting issues you identified about this company.

Exercise Exhibit 1: Selected Risk Factors

1. The Company's reliance on a small number of customers for a large portion of its revenues could harm its business and prospects. A number of contracts held by those customers may be terminated at the customer's discretion.

2. The Company's business is dependent upon governmental policies and appropriations.
3. The Company's lengthy sales cycle requires it to incur significant expenses with no assurance that it will generate revenue or recover such expenses.
4. The Company conducts its business worldwide, which exposes it to a number of difficulties in coordinating its international activities and dealing with multiple regulatory environments.
5. The Company's reliance on a limited number of suppliers for some key components for its products could harm its business and prospects.
6. The Company could incur substantial costs as a result of product liability claims and adverse publicity if its products fail to do what they are supposed to do. (reworded by me).
7. The Company's success depends on new product development.
8. The Company's success depends upon its ability to adapt to rapid changes in technology and customer requirements.

Exhibit 3

EMBA GROUP EXERCISE – February 12, 2010

February 9, 2010, Washington, D.C.

US lawmakers called upon the CEO of Wellpoint, Inc. to testify before Congress concerning a proposed 39% increase in premiums at its California operations. Hearings will be held on February 24th before the House Energy and Commerce Committee. Given your reputations as impartial experts in financial analysis, both Committee Chair Henry Waxman (D-California) and Wellpoint CEO Angela Braly have asked you to analyze the financial statements of the company and present your findings. You are to look for any interesting points you can find. You may fully use the internet as well as the Dec. 31, 2009 financial statements that your ace research assistant Sharon has pulled together and summarized.

Industry ratios: Medical loss ratio = Benefits paid/premiums received

Helpful websites:

- <http://www.investopedia.com/articles/stocks/09/investing-in-health-insurance.asp>
- <http://www.sec.gov/Archives/edgar/>

data/1156039/000119312510013601/dex991.htm

- http://www.sec.gov/Archives/edgar/data/1156039/000119312509033022/d10k.htm#toc55443_2

Exhibit 4

FINANCIAL REPORTING AND ANALYSIS EMBA GROUP EXERCISE – January 29, 2010

Assignment

1. Scan the attached financial statements and other materials associated with two major competitors in the same industry. Point out clues to the type of industry this might be (sales, service, financial, capital intensive, heavily/lightly leveraged, profitable/not, etc.) [Note the different year ends. I did not include any quarterly statements in this exercise, but both companies have continued doing reasonably well since these last statements.]
2. Note the first column for each company on the income statement contains “common-sized” information. For the income statement, all the other items are stated as a percentage of total revenues; the balance sheet, all other items are as a percentage of assets. Study the income statement first, noting the major expenses and differences between the two companies. What factors could cause expenses to be different for companies in the same industry? Do the same type of analysis on the balance sheet.
3. The following page contains formulas for common financial analysis ratios. Calculate them for each company for the most recent year.
 - a. What does the PE ratio mean? Which is better? Why would they be different?
 - b. Which company is most liquid? Can most easily meet its current obligations? What factors would affect how liquid a company or industry should be?
 - c. Do the companies differ much in their average days in receivables? Why might that be?
 - d. Which company is most highly leveraged? Any thoughts?

4. Alpha Company has a book value (Assets – liabilities) of \$6.8 billion. Omega has a book value of \$6.3 billion. Contrast that to what the stock market thinks the value of each company to be. Why would they be so different?
5. Read the Risk Factors reported by both companies in the 10ks. Do you know who they are yet without Googling everything on the next page?
6. How does this exercise integrate what you are learning in financial reporting with your marketing and economics classes?

SOME COMMON RATIO CALCULATIONS

1. Current ratio:
 $\text{Current assets} / \text{Current liabilities}$
2. Quick ratio:
 $(\text{Current assets} - \text{prepaids} - \text{inventories}) / \text{Current liabilities}$
3. Accounts receivable turnover:
 $\text{Sales} / \text{Average accounts receivable (in times per year)}$
4. Days in receivables:
 $365 / \text{Accounts receivable turnover}$
5. Price/Earnings ratio:
 $\text{Market price per share} / \text{Earnings per share}$
6. Debt/Assets ratio:
 $\text{Total liabilities} / \text{Total assets}$

RISK FACTORS FOR COMPANIES IN THIS INDUSTRY

1. Our business depends on our strong reputation and the value of our brand.
2. Labor organizations attempt to organize groups of our employees from time to time, and potential changes in labor laws could make it easier for them to do so.
3. We rely heavily on technology to operate our network, and any disruption to the infrastructure or the Internet could harm our operations and our reputation among customers.
4. Our business may be impacted by the price and availability of fuel.
5. Our business is capital intensive, and we must make capital expenditures based upon projected volume levels.

6. We face intense competition, especially during the current global recession.
7. Increased security requirements could impose substantial costs on us.
8. The regulatory environment for global aviation rights may impact our air operations.
9. We may be affected by global climate change or by legal, regulatory or market responses to such change.
10. We are directly affected by the state of the economy.
11. Strikes, work stoppages and slowdowns by our employees could adversely affect our business, financial position and results of operations.
12. Employee health and retiree health and pension benefit costs represent a significant expense to us.