A Compilation of Accounting Case Studies and Analyses

by
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ABSTRACT

MADISON HUEY: A Compilation of Accounting Case Studies and Analyses

(Under the direction of Victoria Dickinson)

Over the course of two semesters I completed twelve case studies under the direction of Dr. Victoria Dickinson. Each of those cases is presented here to serve as my Honors Thesis. They are accompanied by brief analyses to show my understanding of each topic covered in the case. In addition to the completion of case studies, I also had the opportunity to attend twelve presentations from Big 4 firms. During these presentations, I learned the values of each firm and had the opportunity to network with professionals from each firm. Furthermore, I participated in two case competitions, during which I was required work with a team to use critical thinking and problem solving skills to solve particular financial problem. Once we determined the best course of action, my team and I presented our analysis and solution to firm management. Each of these opportunities and the direction of Dr. Dickinson ultimately lead me to my senior accounting internship, which I completed with PwC in Dallas. I have accepted a full-time job offer with this firm and will start in 2020 once I have received my Master’s of Accountancy: Data and Analytics from the Ole Miss Patterson School of Accountancy.

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Introduction and Analysis

Similar in location, operations, and product, Glenwood Heating, Inc. and Eads Heater, Inc. began operations in year 20X1. Both companies sell home heating units and conduct identical yearly operations. Furthermore, because they function in the same industry, they face similar economic conditions, challenges and opportunities. Although the two companies are very similar, they differ in how they are managed. Each company has its own distinct way of adhering to generally accepted accounting principles (GAAP). This means that their prospective financial statements will have an overall similarity but will ultimately be distinguishable due to difference in accounting methods. For example, the two companies use two separate methods of recording inventory and thus cost of goods sold. Glenwood Heating, Inc. uses the first in first out (FIFO) method while Eads Heaters, Inc. uses last in last out (LIFO) method.

The subsequent data concerning this particular difference can be found in the companies' income statements. Glenwood has a cost of goods sold of $177,000 while Eads has $188,000. This difference is most likely due to a rise in cost of the product over time. As a result, Glenwood has both a higher gross profit and net income. However, Glenwood also has a higher income tax. Another accounting difference is the estimate of bad debts for each company. Glenwood uses only 1 percent, while Eads uses 5 percent. This difference is noted in the balance sheets of the companies. Furthermore, Glenwood and Eads determine depreciation, an expense taken from profit and a deduction in the value of equipment, using different methods. This difference can be found in both the income statements and balance sheets, respectively. To depreciate delivery equipment, Glenwood uses the straight-line method while Eads uses the double-declining balance method. This means that Eads depreciates delivery equipment at a faster pace than Glenwood, causing depreciation expense to be higher and value of the equipment to be lower. The companies also have a difference in equipment rental negotiations. Glenwood rents a piece of operating equipment every year while Eads negotiated a capital lease agreement with the owner of the equipment. This means that Eads carries this equipment on its balance sheet while Glenwood does not. Furthermore, Eads also depreciates this equipment.

If I were to invest in one of the two companies featured in this case, I would most likely invest in Glenwood Heating, Inc. Glenwood implements a less conservative approach and therefore, reports higher net income and retained earnings. This leads to higher ratios than Eads. For example, Glenwood's current ratio is 3.04 while Eads' is 1.12. Furthermore, Glenwood's profit margin on sales is .23 while Eads' is .18. Analysts and users of financial statements look at ratios like these to determine whether or not to invest in a company. I believe that Glenwood is more likely to have investors and buyers of stock based on their reports. Stock prices will continue to rise because of potential for future cash flows evidenced by improved ratios. Therefore, they will have the capacity to grow and become even more successful. Although it is worth mentioning that Eads has more cash on hand, I would still ultimately invest in Glenwood Heating, Inc.