Accounting & Accountability

SSc2022

University College Maastricht

(period 5)

Course Manual

Maastricht University
School of Business and Economics
Department of Accounting & Information Management
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1. Introduction

Accounting systems have been used for thousands of years. As businesses grew, accounting systems were used to keep track of transactions, costs, profits and losses. Modern accounting systems measure and communicate financial information on an economic entity. This information is used to plan, control, evaluate, and make decisions about a business. The process begins with bookkeeping: recording transactions, such as checks and invoices, and summarizing these transactions in financial statements. Financial managers use the financial statements to raise and spend money and make intelligent financial decisions. So:

- an accounting system is an information system that measures, processes, and communicates financial information about an identifiable economic entity;
- bookkeeping, primarily a mechanical and repetitive record keeping function, is a subset of accounting;
- finance is concerned with raising and investing money;
- an accounting system provides information about the company to financial managers so they can make intelligent financial decisions;
- accounting enables managers to intelligently plan and control the business and make decisions based on objective information.

Typically, a distinction can be made between financial accounting and management accounting, the latter often complemented by management control. Both forms of accounting need information extracted from the financial information system.

In discussing the subject of management accounting, which has an internal focus (providing information for managers and the board of directors), we will concentrate on the value of management accounting information for the internal decision-making process. In general, the purpose of management accounting is to facilitate decision-making (e.g. cost calculations, and pricing) and to influence decision-making (e.g. performance evaluation and executive compensation). For instance, management accounting information is used to formulate plans and analyze the gap between plans and realizations. This information can then be used to try to close these gaps. A management accounting system incorporates different types of financial and nonfinancial information from a wide range of sources. Several concepts within the field of management accounting will be illustrated.

In financial accounting, the external use of accounting information is discussed. The most important outcome of the financial reporting process is the annual report (or the semi-annual or quarterly report). Besides management's discussion of the firms performance, strategy, corporate governance, risk management, et cetera, an annual report contains the firm's financial statements and the notes to these financial statements. Much discussion in the business press relates to information from these financial statements. For example, the performance of a firm during a period is often judged by its net income.

Unlike management accounting, financial reporting is governed by financial reporting standards. In the U.S. these standards are called U.S. GAAP (generally accepted accounting principles). Listed firms in the European Union have to follow IFRS (International Financial Reporting Standards). This course will introduce the basic principles of financial accounting and reporting that are largely similar under these two sets of standards. Understanding these basic principles underlying 'the language of business' is essential to anyone who will be involved in the preparation (e.g. controllers), monitoring (e.g. supervisory board members, auditors, stock market regulators), analysis (e.g. financial analysts, M&A consultants), or use (e.g. venture capitalists, governments, private shareholders, bondholders) of financial accounting information.

However, firms also have the freedom to make their own financial reporting decisions, because financial reporting standards leave firms considerable flexibility. For example, as will be illustrated in this course, firms have to choose how they will value their inventories and what method they will use to depreciate their long-lived assets. Managers enjoy flexibility in financial reporting so that they can give an accurate picture of their firm's performance and financial position. However, this flexibility can also be misused to the firm's or the manager's own advantage as illustrated by the wave of accounting scandals of the early 2000s (e.g. Enron, Parmalat, Ahold). These scandals have shown the importance of high quality financial reporting to financial markets. Also, they have led to a strengthening of rules concerning management's responsibility for their firm's financial reporting, internal control, auditing, and corporate governance.

A topic of special importance in accounting and accountability nowadays is corporate governance. In essence, corporate governance deals with the relationships between a company's management, its board, shareholders and other stakeholders.

Throughout these developments, accounting has evolved from an entirely financially oriented discipline to one that also studies non-financial information, leading to such contemporary concepts as the balanced scorecard, and corporate social reporting. This course follows that contemporary, broad – hence including non-financial information – notion of accounting.

2. Course coordination and objectives

The course Accounting & Accountability is coordinated by Bas Braakhuis, lecturer at the department of Accounting & Information Management (AIM) of Maastricht University School of Business and Economics (SBE). This course is built by multiple coordinators and their input is highly valued. For questions, remarks and/or suggestions, please contact me via e-mail: s.braakhuis@maastrichtuniversity.nl

This course provides a broad overview of the main accounting topics, ranging from conventional topics, focusing on financial information, to more contemporary subjects, emphasizing the role of accounting and accountability in modern society. Students that have followed this course should be able to:

- Apply basic bookkeeping techniques (making journal entries and preparing basic financial statements);
- Apply basic management accounting techniques (e.g. cost analysis, budgeting);
- Understand the basics of auditing and management control;
- Understand international accounting rules and principles;
- Understand the causes and implications of current accounting events, such as accounting scandals (e.g. Enron, WorldCom), and corporate governance codes (e.g. Sarbanes Oxley);
- Understand developments in corporate governance
- Understand the role of accounting in business/society-issues.

3. Literature

Given the fact that the vast field of accounting and accountability is not covered by a single text book, selected chapters from the following text books will be used:

- Management Accounting:[1]
  Bhimani, A., C.T. Horngren, S.M. Datar, G. Foster (2008/2012). *Management and Cost Accounting*, Prentice-Hall, 4th, 5th or 6th edition.[2]
- Financial Accounting:
  Harrison, W.T., C.T. Horngren, C.W. Thomas & T. Suwardy (2010). *Financial Accounting – International Financial Reporting Standards,* Pearson, 8th or 9th (global) edition.
- Corporate Governance:[3]
  Kim, K.A., J.R. Nofsinger & D.J. Mohr (2010). *Corporate Governance (International Edition)*, Pearson Education: Upper Saddle River, 3rd edition.
- Auditing:
  Knechel, W.R., S.E. Salterio, & B. Ballou, (2007). *Auditing: Assurance & Risk,* South-Western, 3rd edition.
- Management Control:
  Drury, C. (2005). *Management Accounting for Business*, Thomson, 3rd edition.

Several copies of these text books are available in the University Library. Next to these main text books a number of (research) articles and other publications will be used. The compulsory additional literature can be found on the Student Portal and/or via (the website of) the University Library. In addition, a hardcopy reader will be available in UCM's Reading Room, as well as copies of both the Financial and Management Accounting text book.

Please note that it is not mandatory to buy all these text books, since only a (small) number of chapters will be covered, as expressed in the following schedule:

Topic	**Main author**	**Chapters covered**
Management Accounting	Bhimani	1+2+3+5+8+9+11+14
Financial Accounting	Harrison	1+2+3+6+7
Corporate Governance	Kim	1 + 2 + 4
Auditing	Knechel	1 + sections from 2, 3, 4
Management Control	Drury	11

[1] In the University Library you can also find other books that cover management accounting:
- Drury, C. (2016). *Management and Cost Accounting*. Thomson, 6th edition.
- Horngren, C.T., G. Sundem, W. Stratton, D. Burgstahler & J. Schatzberg. (2008) *Introduction to Management Accounting (International Edition)*, Prentice-Hall, 14th edition.

[2] The 4th and 5th and 6th edition of Bhimani's *Management and Cost Accounting* are essentially the same, and can be used interchangeably. The course's hard copy reader contains photocopies of the 6th edition, therefore page references contained in this course manual relate to the 6th edition. From the 6th edition these page references are as follows: Chapter 1 pp.2-15; ch.3: pp.59-66; ch.5: pp.123-131 + 139-141; ch.7: pp.178-190; ch.9: pp. 244-254 + 256-258;; ch.14: pp.424-439..

[3] More detailed Corporate Governance text books can be also be found in the University Library:
- Monks, R. A. G. & Minow, N. (2008). *Corporate governance*. John Wiley and Sons, 4th edition.
- Tricker, B. (2009), *Corporate Governance: Principles, Policies and Practices*, Oxford: Oxford University Press

NOTE: Some download links in this course manual or on the course Student Portal website (i.e. via EBSCO) may require a connection from a UM-based computer or Student Desktop Anywhere or, if downloaded from your home computer, a VPN connection to the UM network.

4. Course structure

The course will be offered in Maastricht University's usual PBL format and will – according to the provisional scheduling of the course – consist of 11 meetings in 7 weeks.

During the tutorials, the required tasks and exercises will be analyzed and discussed. A couple of meetings – tasks marked by a double asterisk (**) – will feature presentations (of appr. 45 minutes) by subgroups of students (of which 3 contain a case discussion).

Presenting teams are required to provide additional information next to the contents of the compulsory literature for their particular subject. Furthermore, as part of the presentation, the presenters have to lead a discussion in the tutorial group on the subject of their presentation. In order to engage in a meaningful discussion, every student has to prepare the literature and – when asked for – be able to summarize its core messages.

Although the design, structure and setup of the presentations are up to you, it is important that you make the presentation interactive, i.e., that you actively involve the group members in the discussion of the literature. One way to achieve this is by incorporating intermediate discussion topics in the form of questions and/or statements related to the literature that lead to class discussion. In addition to the materials from the assigned literature, you are free to use any newspaper articles, anecdotes, as well as relevant pictures, short video clips, etc. to make the presentation as active, lively and practical as possible.

In addition to contributing to the aforementioned group discussion, the remaining students should afterwards be able to give constructive feedback on the presentation. A number of students will be asked to evaluate the presentation of their peers using the presentation evaluation form given in the appendix of this course manual.

Presenters are requested to hand in a digital version and/or hard copy of their presentation to the tutor before the meeting. Afterwards, the presentation has to be posted on the tutorial's discussion board, so all students can review the contents of the presentations, which may be relevant for the exam as well. Feel free to also upload any digital notes for your presentation to the discussion board to help your fellow students prepare for the exam.

The compulsory literature and corresponding tasks and presentations are listed in the course overview on the next page.

5. Course overview

Meeting	Topic	Literature	Preparation (tasks to be post-discussed, presentations)
1	Introduction	FA: ch.1 MA: ch.1*	Task 1
2	Financial & Management Accounting Financial Statements	FA: ch.1+2	Task 2+3
3	Transaction Analysis & Accrual Accounting	FA: ch.3+6	Task 4+5
4	Inventory & Long-term assets	FA: ch.7	Task 6a+6b
5	Preparing the Financial Statements	FA: ch.1+2+3+6+7	Task 7 + Q
	To be announced MID TERM EXAM – FINANCIAL ACCOUNTING		
6	Cost Analysis	MA: ch.2 & 3*+9*	Task 8+9
7	Cost Allocation & absorption/variable costing	MA: ch.5*+7*+11	Task 10+11
8	CVP + Budgets+ practice questions Management Accounting	MA: ch. 8 & 14*	Task 12 + 13 + Q
9	Management Control Auditing	Drury ch.11* + *case* Knechel (selection) + *case*	Task 14** (+ case) *PRESENTATION Management Control* Task 15** (+ case) *PRESENTATION Auditing*
10	Corporate Governance	Kim&Nofsinger (ch.1+2+4) Smith (article) Friedman (article) *WorldCom case*	Task 16** *PRESENTATION Corporate Governance* Task 17** (WorldCom case) *PRESENTATION WorldCom case*
11	A Framework for Accounting and the Financial Crisis + practice questions final exam	All previous literature + case study	Case to be announced *PRESENTATION Internal control/auditing* *+Q*
	Final Exam		

Text book chapters marked by a single asterisk (*) only need to be studied to the extent indicated in the relevant task. Tasks marked by a double asterisk (**) relate to the subgroup presentation in those tutorials.

6. Examination

To realize the full benefits of a PBL environment it is essential that students are actively involved in class discussion. Preparation, attendance and participation are therefore prerequisites for optimal group functioning. Consequently, every student will be graded on his/her individual participation in every meeting. Preferably, your in-class contributions reflect thorough preparation. However, feel free to ask for clarifications from fellow students. A rough indication of the grading system for participation is as follows:

- Outstanding: active participation in all meetings, contributions reflect thorough preparation and are well-argued, contributions guide class discussion (grade: ≥9)
- Good: frequent participation, student is well prepared, contributions are mostly substantive, and sometimes provide direction for class discussion (grade: 7-8)
- Adequate: participation varies between sessions, contributions reflect adequate preparation, but are only sometimes substantive (grade: ±6)
- Non-participant: has said little or nothing in class, therefore hardly any basis for evaluation, does not have any effect on the quality of class discussion. (grade: 4-5)
- Unsatisfactory: contributions demonstrate inadequate preparation, and provide few if any insights; comments are isolated, possibly confusing (grade: 4)

In accordance with UCM regulations, students have to attend at least (approximately) 85% of all group meetings to pass the course. If you have missed more than 15%, but no more than 30% of all meetings, you have to prepare – and receive a passing grade for – an additional assignment in order to meet the attendance requirement. The nature and volume of the additional assignment will be proportional to the number of meetings missed. Please take into account that this additional assignment might therefore require a substantial workload. If you missed more than 30% of all meetings, you cannot receive a passing grade for this course. As the course will consist of 11 meetings you will have to attend at least 9 out of 11 group meetings to pass the attendance requirement.

Furthermore, students will have to prepare 1 subgroup presentation related to the course contents. More information on the requirements for the presentations can be found in the relevant task (task 14, 15, 16, 17, 18) and in section 4 of the course manual. A rough indication of the grading system for presentations is as follows:

- Outstanding: presentation is well-structured, slides add value to the presentation, required literature is discussed in an integrated matter and coupled with interesting additional materials, class discussion is stimulated by interesting discussion questions, questions are answered convincingly, presentation style is outstanding (grade: ≥9)
- Good: presentation is appropriately structured; covers all required readings, but might lack emphasis on important elements; class discussion is stimulated adequately; good presentation style (grade: 7-8)
- Adequate: elements of required literature are discussed but mostly in isolation, presentation lacks any real added value, hardly stimulates class discussion, presentation style needs improvement (grade: ±6)
- Unsatisfactory: presentation lacks a clear structure, important elements of required literature are not covered, provides no room for class discussion, presentation style is insufficient (e.g. merely reading slides out loud) (grade: ≤5)

Finally, the **course will consist of 2 exams.** The **financial accounting part** of the course **will be concluded by a <u>mid-term exam</u>.** The **remaining course content** will be **tested in the <u>final exam</u>.** Both exams will be written closed-book exams consisting of a combination of multiple choice questions and open questions, and will be graded on a scale from 1 to 10.

The mid-term exam will take place in week 3 or 4 of period 5. The final exam will take place in the last week of period 5.

The final grade for this course will be determined as follows:

Mid-term exam	30%
Final exam	45%
Individual participation	10%
Subgroup presentation	<u>15%</u>
Final grade	100%

In order to pass this course, a final grade of at least 5.5 must be obtained.

The <u>resit exam</u> will cover <u>all</u> course contents previously tested in both the mid-term and the final exam. Taking part in the resit is only allowed after completing all the requirements (the mid-term exam, the final exam, class participation and the subgroup presentation) of the course, and if the average grade based on those 4 parts is less than 5.5. The grade of the resit exam will replace the grades of the 2 prior exams, but <u>not</u> the grades for individual participation and the subgroup presentation. The resit exam will take place in the Spring semester resit week.

7. Code of Conduct

Because this course is offered by the School of Business and Economics' department of Accounting & Information Management (AIM), the following code of conduct – composed by AIM department chair prof. dr Ann Vanstraelen – is applicable:

"I expect the coordinators, tutors, and students in this and other Accounting & Information Management courses to behave in a manner that is suited in general and for an academic institution in particular. I emphasize fairness to all students taking the course. Please do not do anything that is unfair to other students, or ask the coordinator/tutor to make exceptions that are unfair to other students. In addition, do not perform activities that have the effect or intention of interfering with education or fair evaluation of a student's performance. Examples of such activities include, but are not limited to:

1. *Cheating: behaving in a dishonest or deceitful way in order to win an advantage.*
2. *Plagiarism: copying another person's work, ideas, etc. and submitting it as your own or without attribution.*
3. *Fabrication: using fictitious data and results with the sole purpose to deceive.*
4. *Misrepresentation of records: tampering and falsifying information, for example on one's resume.*
5. *Facilitating dishonesty: knowingly helping or attempting to help another violate any of the above provisions.*

Furthermore, in communicating with the academic staff and fellow students, you are expected to behave in a courteous way, i.e., you are expected to show good manners and respect for others. You are especially advised to take this into account in your email communication. The mere fact that the development in information technology has made it possible to send an email within a split second does not mean that you should do so. Think twice before you send an email!

Adhering to the above code of conduct ensures that we can all focus on the fundamental purpose of an academic institution, which is the pursuit of knowledge."

Prof. dr Ann Vanstraelen
Chair of the Department of Accounting & Information Management (SBE)

8. Tasks

Task 1 Financial and Management Accounting

While studying business, three students named Jack, Marie, and Jane want to try their luck and open up a sandwich bar – Something Better – that provides quick and cheap food for students. They want to serve sandwiches, burgers, and drinks. Furthermore, they want to start a lunch delivery service that serves student conferences, for example.

The three students are engaged in a discussion about how accounting can help them in the management of their business. "First, we should think about what kind of form our business should take", Jack begins. "A proprietorship? A partnership? Or whatever other form a business can take?"

"We should also think about recording our financial transactions in an accounting system", says Jane. "I don't see how recording our financial transactions can really help us", Marie responds. "Wait a minute", Jack interrupts, "recording transactions is only one thing; accounting is more than bookkeeping. The major goal of accounting is the use of the information." "Use? The only use I can think of, is having an overview of the amount of money we can spend and the amount of products in stock; is that worth the effort of recording every transaction?" says Marie. Jack counters: "The management of Something Better – that is: the three of us – should use the accounting information for all kinds of decision making. And besides internal uses, external parties will also use the information." "Isn't that what the difference between management and financial accounting is about?" Jane adds. "External parties will use the accounting information!? I don't want other people to look over my shoulder! Besides, there may be private information included in Something Better's records. The balance in my private savings account is none of anyone's business!" Marie says agitatedly. Jack, with a tiresome look in his eyes: "Marie, have you ever heard of the concept of separate entity?"

Additionally, they try to figure out the distinctions between management accounting and financial accounting by using the following 4 characteristics a) reporting interval; b) the impact of regulations; c) time period; and d) range and detail of information. Furthermore, Jack argues that, irrespective of the differences, both accounting forms are necessary for a well-functioning business and require an accounting system.

"Coming back to your point about external reporting, we should follow IFRS" Jane adds. "But who checks whether one applies those standards and principles correctly?" Jack wonders. "If everyone who prepares financial statements just interprets accounting standards in their own way, there is no way to compare different companies."

Literature: *Harrison et al. (FA), chapter 1*

Bhimani et al. (MA), chapter 1

(pp. 2-15)

Task 2 Financial Statements

Marie, Jack, and Jane continue their discussion about the necessity of financial reporting for Something Better. Jane searches the internet for the annual reports of other companies and finds out that the financial statements are comprised of four different statements. She decides to print out the financial statements of an exchange-listed fast food chain called *SuperSandwich*, a big future competitor of Something Better.

Marie wonders what the purpose of the different financial statements is. Jack immediately starts to search for the relationship between the different statements, but gets stuck. He remembers something about the 'accounting equation', but decides to dig into his introductory financial accounting textbook. After studying, he decides to test his friends' knowledge of the relationship between the different financial statements by crossing out a few numbers on Jane's print-out and seeing whether they can fill in the blanks. Furthermore, he wonders what all the terms mentioned in the financial statements mean, and whether he can think of examples of those in relation to their sandwich shop.

Literature: Harrison et al. (FA), chapter 1

SuperSandwich		
Income Statement for the year ended December 31st 2013, in thousands of €		
Sales revenue		90,000
Cost of goods sold	35,000	
Salary expenses	2,000	
General and administrative expenses	4,000	
Depreciation expense	[redacted]	
Total operating expense		[redacted]
Earnings before interest and taxes		[redacted]
Interest expense		2,000
Earnings before taxes		[redacted]
Income tax expense		16,000
Net income		[redacted]

Supersandwich	
Statement of changes in equity for the year ended 31st December 2013, in thousands of €	
Shareholders' euity, January 1st	[redacted]
Net income	[redacted]
Issuance of common stock	[redacted]
Dividends	(3800)
Shareholders' euity, December 31st	55200

SuperSandwich

Balance sheet for the years ended December 31st 2013 and 2012, in thousands of €

Assets			**Liabilities and shareholders' equity**		
Current Assets	2013	2012	Current laibilities	2013	2012
Cash	[redacted]	6,400	Accounts payable	26,300	22,800
Accounts receivable	9,200	5,900	Income taxes payable	5,900	4,200
Inventory	22,000	19,000	Salaries payable	2,700	2,300
Prepaid expenses	1,400	1,000	*Total current liabilities*	34,900	29,300
Total current assets	[redacted]	32,300			
			Long-term liabilities		
Long-term assets			Bank loan	25,000	20,000
PPE*, at cost	55,000	53,000	*Total long-term liabilities*	25,000	20,000
Accumulated depreciation	13,000	6,000			
PPE*, net	42,000	47,000	Shareholders' equity		
Other assets	2,000	2,000	Common stock	8,000	5,000
Total long-term assets	44,000	49,000	Retained earnings	[redacted]	27,000
			Total shareholders' equity	[redacted]	32,000
Total assets	[redacted]	81,300	***Total liabilities and shareholders' equity***	115,100	[redacted]

SuperSandwich	
Cash flow statement for the year ended December 31st 2013, in thousands of €	
Cash flows - operating activities	
Net income	[redacted]
Depreciation	7,000
Other adjustments to reconcile net income to cash flow from operating activities	-1,100
Net cash provided by operating activities	29,900
Cash flows - investing activites	
Purchases of property, plant and equipment	[redacted]
Sale of property, plant and equipment	8,500
Net cash used in investing activities	-2,000
Cash flows - financing activities	
Issuance of common stock	3,000
Borrowing from bank	[redacted]
Dividends	-3,800
Net cash flow provided by financing activities	4,200
Net increase in cash	[redacted]
Cash at January 1st	[redacted]
Cash at December 31st	[redacted]

Task 3 Transaction Analysis

Although Something Better will only open its business January 5, 2016, a few transactions have already taken place in December 2015. Jane suggests recording these transactions in the journal and general ledger and drawing up a balance sheet of Something Better at December 31, 2015.

- On December 15, 2015 Marie, Jack, and Jane each contributed €2,000 capital to Something Better.
- On December 29, groceries were purchased on account, totalling €1,500, which has to be paid within 30 days.
- On December 30, based on their business plan, they obtained a five-year bank loan of € 12,000 at an annual interest rate of 8%. Interest has to be paid monthly, starting in January 2016.
- On December 31, various store equipment was bought and paid at a total cost of €4,000.

But how do companies keep record of these transactions? Jane remembers something about the double-entry system, journal entries, and T-accounts. She also remembers that there were rules about debit and credit.

Jane decides to record all the transactions for December 2015. For each transaction, she also records each account as an asset (A), liability (L), stockholders’ equity (SE), revenue (R) or expense (E) and indicates whether it increases (+) or decreases (–).

Literature: Harrison et al. (FA), chapter 2

Task 4 Accrual accounting and financial statements

For Something Better the first month in business has ended (see task 3). In January 2016 the company was engaged in the following activities:

- January 2, monthly payment of interest on €12,000 bank loan (8% annual interest rate).
- On January 3, a store location was found and four months' rent was paid in advance, totaling €1,200.
- January 5, bread and groceries were bought and paid, totaling €800. Drinks were bought on account for €300.
- January 23, payment of the bread and groceries bought on December 29, 2015 for €1,500.
- In total, cash sales of €2,600 were made. In addition, sales on account were €400.

Heat and light expenses are estimated at €150 per month, but these don't have to be paid until the end of every 3-month period. The friends estimate that the equipment bought at the end of December 2015 for €4,000 has to be replaced after 3 years. On January 31 the value of the inventory (bread, groceries and drinks) is €600.

Jane records these transactions by preparing journal entries (including adjusting entries) and T-accounts, and prepares the balance sheet of Something Better on January 31, and an income statement. On February 1, the three friends are interested to measure the success of their company's operation for the month of January. Jane remembers that a company's performance can be assessed by evaluating profit figures (using the accrual approach) or cash flows (using cash-basis accounting). She also remembers that one of the methods requires to account for accrued and deferred revenues/ expenses. Marie suggests that they assess the performance of their company using both methods. After they have done so, Jack is confused. Jane is wondering whether the so-called revenue recognition and matching principle can explain the different outcomes and which of the two methods is to be preferred.

Literature: Harrison et al. (FA), chapter 3

Task 5 Inventory

Inventory management is very relevant for many companies. As something better is a small sandwich shop with low levels of inventory (because everything needs to be as fresh as possible), there are more interesting cases to look at. Therefore, we take a look at Bookmarker, another student company that sells new and second hand books in order to provide students with a cheaper alternative to the current academic bookstores.

Most of the books Bookmarker sells are bought from publishers. The price of these books is set by the publisher and this price can change based on popularity of the book, printing costs, number of books bought, et cetera. During 2011, the following transactions have occurred for a book by Dan Brown.

Transaction	**Units**	**Unit cost (€)**
Beginning inventory	30	8
February 5: Purchases	10	10
July 12: Purchases	10	11
September 20: Purchases	10	12

One of their owners, John, wants to know the gross margin for Bookmarker for this title as well as the value of the ending inventory. He can easily calculate total sales for this title, because he knows that 45 books were sold during 2011 at a price of €20, but he is not sure what number he has to use for the cost of goods sold. He knows this number depends on the inventory costing method used. Looking in his accounting text book, he quickly realizes that a cost-benefit trade-off will show that the specific identification method is not useful for Bookmarker. However, he sees that there are three other methods that he can use. He makes a table to compare the results for all three methods. More specifically he wants to compare sales revenue, cost of goods sold, gross margin, and ending inventory. What method should he prefer?

John also found out that accounting standards require companies to value their inventory at the lower of cost and net realizable value. For example, what write-down would he have to make to the value of ending inventory if, after the 2011 Christmas period, the book of Dan Brown could only be sold at, say, €9 per copy?

Literature: Harrison et al. (FA), chapter 6

Task 6a Long lived assets

For a moment we forget about our friends at Bookmarker and go one link back in the value chain to look at the book printer 'Smeets Printing'.

Smeets Printing has bought a machine that improved both the speed of printing as well as the quality of the printed books. The price of the machine was €2,000,000 with an estimated useful life of 10 years and an estimated residual value of €100,000. The company expects that 80,000 books will be printed in each of the first 5 years with this machine and 60,000 books in each of the last 5 years.

The controller of Smeets Printing knows the purpose of depreciation but has to decide which depreciation method the company will use for this machine. He starts working out the different scenarios and wonders which method he should use.

During the years there have been a number of repairs on the machine. The controller does not know whether he should capitalize these costs or not: "On the one hand", he thinks, "these are costs for a capitalized machine, so I should capitalize all costs. On the other hand however, the economic useful life of the machine did not increase."

After using the machine for 6 years a new and even better machine is developed in the market. Smeets Printing decides that it will sell the current machine for €750,000 and buy a new machine for €3,000,000. The controller of Smeets Printing has used the straight line depreciation method for the old machine.

Task 6b Intangible assets

Over at Something Better, Marie is thinking that not all of a company's assets exist in a tangible form. Many assets are intangible, like research and development, patents, employee knowledge, brand names, goodwill, and a company's reputation. However, when she looks at the annual report of their big competitor, SuperSandwich, she does not see all of these items in the financial statements, and wonders why. Furthermore, she wonders how companies account for their intangibles and how they deal with the fact that tangible assets have economic lives that are easily estimable, whereas many intangibles have indefinite lives.

She decides to ask Jack what the difference is between accounting for tangible and intangible assets. "I do not think the difference is that important. The only difference is that depreciation is called depletion", Jack replies: "or was it amortization?" Jane overhears their conversation and remembers something about 'impairment' of intangibles, but she is not sure herself.

<u>*Literature:*</u>

- *Literature: Harrison et al. (FA), chapter 7*
- *Summary of IAS 38 - Intangible Assets. Downloadable from: http://www.iasplus.com/standard/ias38.htm*

Task 7 Preparing the Financial Statements

Time flies and Jack Marie and Jane are now in business for one year. After enjoying a short Christmas holiday, our friends come back to the sandwich bar on January 2, 2016 and they are curious about their performance in their first year of business. They know that they have to prepare the financial statements for 2016 now. Jane gets the unadjusted trial balance printed from Something Better's accounting system:

Something Better

December 31, 2016, all numbers are in €

	Unadjusted trial balance		Adjustments		Adjusted trial balance	
	Debit	Credit	Debit	Credit	Debit	Credit
Cash	13,450					
Accounts receivable	800					
Accrued advertising revenue						
Inventory	1,300					
Prepaid rent	2,500					
Equipment	8,600					
Accumulated depreciation		1,200				
Total	**25,450**					
Accounts payable		600				
Salaries payable						
Income tax payable						
Interest payable						
Bank loan		15,000				
Share capital		4,500				
Retained earnings		0				
Total		**20,100**				
Sales revenue		50,000				
Service revenue						
Cost of goods sold	27,000					
Heat and light expense	1,350					
Salary expense	9,600					
Interest expense	1,000					
Depreciation expense	1,200					
Rent expense	4,500					
Income tax expense						
Total		**5,350**				

The trial balance takes into account transactions over 2016 that are already recorded in the accounting system. However, there are some transactions that are not yet recorded and for which Jane still has to make adjusting entries. She gathered the following information:

1. Part of the equipment has been bought in December 2016 for €3,600. This equipment is depreciated using straight line depreciation. Jane has already recorded the depreciation on this machine for 2016. However, on October 1, 2016, additional equipment was bought for €5,000, which is depreciated using the double-declining balance method. The depreciation on this machine has not been accounted for yet. It is expected that this additional equipment has to be replaced after five years and has no residual value.
2. Study association *Scope* still has to pay €720 for putting advertisement posters for their activities on the billboards in the Bookshop. The Bookmarker records these revenues as service revenue.

3. On October 1, €2,500 rent was prepaid for 5 months. Rent expense has been booked for the first three quarters of 2016.
4. Salaries for the first half of each month are paid around the 20th of the month; salaries for the second half are paid around the 5th of the following month. Salaries have been administered up to and including the first half of December. The salaries of the second half of December, amounting to €400, will be paid in January 2016.
5. The bank loan is a €15,000 five-year bank loan at an annual rate of 8%. The Bookmarker changed the arrangements with its bank and now pays interest only once a year on October 31. Interest has not yet been accrued for November and December 2016.
6. Heat and light expenses are €150 per month. The bill for the October, November and December is paid on December 31.
7. The corporate income tax rate is 25%. These taxes will be paid in 2016.

Using the adjusted trial balance, Jane wants to prepare Something Better's income statement and balance sheet for 2016.

Literature: Harrison et al. (FA), chapter 1, 2, 3, 6 and 7

Management Accounting

Task 8 Cost Terms in Management accounting and Job costing

To set competitive prices for their products, Jack, Marie and Jane need to know the cost of producing their products and services. Having no prior experience, they borrow a book from the library and find a chapter on cost calculations. However, they are not sure about the meaning of different terms such as cost objects, direct and indirect costs, cost accumulation, cost assignment, cost tracing, cost allocation, cost drivers, fixed and variable costs, unit costs, overhead costs, product cost, inventoriable and period costs, and something called relevant range; and how some of the costs of their business might be related to these terms. They are wondering if these terms are really helpful in determining the costs of their products and what the relationship is between the different terms. Furthermore, they become especially confused after reading that variable costs are fixed in units but variable in volume; and fixed costs are variable in units but fixed in volume

From their Accounting book, Jack, Marie and Jane vaguely remember concepts like job costing and process costing. To learn a bit more about these two costing methods, Jack is wondering how he should determine the cost of the lunch delivery that they recently made for the Maastricht Consultancy Days. For that delivery they incurred the following costs:

- 200 sandwiches with an average cost of € 1
- 100 drinks with an average cost of € 0.70
- 2 hours of work for delivering the food, setting up the buffet and cleaning up

Furthermore, he had to drive 10 km (round trip), since the seminar did not take place at SBE. The transportation costs are €0.20 per kilometer. Moreover, every lunch delivery should contribute to covering a range of indirect costs of the delivery business (for example, the cost of the delivery van and advertising costs) that amounted to €1500 this month. Jack decides to allocate these costs based on the amount of time he spent on this delivery, compared to the total time he spent on all deliveries in that month (30 hours).

After his calculations, Jack wonders whether they relate to an actual or normal costing approach, and how some terms he vaguely remembered from the book – cost pool and cost-allocation base – relate to his calculations.

Literature: Bhimani et al. (MA), chapter 2 & 3 (pp. 59--66).

Task 9 Cost behavior

Something Better (SB) incurs several costs that are not directly related to preparing the sandwiches. These costs are related to cleaning and maintaining the kitchen and appliances. In order to keep track of the costs, the accountant kept an overview of the amount of indirect costs, the number of sandwiches produced and sold and the direct labour hours that were needed to produce the sandwiches. During the last 12 months, SB produced 59,260 sandwiches, the labour hours amounted to 827 hours, and incurred total indirect costs equal to € 4,315. More details are given in table 1 below.

Month	Indirect costs	(1) Cost driver: Number of sandwiches	(2) Cost driver: Direct labor hours	**Month**	Indirect costs	(1) Cost driver: Number of sandwiches	(2) Cost driver: Direct labor hours
January	€ 390	4760	66	July	€ 360	3900	43
February	€ 440	6160	88	August	€ 285	3220	49
March	€ 335	4340	69	September	€ 350	5740	81
April	€ 305	5040	77	October	€ 395	6580	59
May	€ 320	4200	91	November	€ 275	4760	67
June	€ 495	6720	40	December	€ 365	5460	86

Table 1: Cost (driver) data for 12 months period

As the indirect costs affect the profit of SB, the accountant sent his overview to Jack, Marie and Jane. They are wondering what they can do with this information. Why would it be important to have cost behaviour information? They start to analyse the indirect cost behaviour. They started with plotting the data but then get stuck. They are wondering whether there are any sophisticated methods to analyse cost behaviour. Marie recalls something about the high-low method, and proposes to apply it to their data, while Jane wonders which one is the best cost driver, and which criteria can be used to evaluate that.

Literature: Bhimani et al. (MA), chapter 9 (pp. 244-254 + 256-258).

Task 10 Cost Allocation and Activity-Based Costing

Something Better (SB) produces two kinds of sandwiches: regular and special. Jack is currently working on product cost calculations for these two products. The direct materials include bread, vegetables, cheese & sauces. The specialty sandwiches also require a special ingredient. Standard product cost calculations are provided below.

REGULAR SANDWICH	QUANTITY	PRICE	COST PER UNIT
Bread	1/unit	€ 0.65/piece	€ 0.65
Vegetables	25 grams/unit	€ 4/kg	€ 0.10
Cheese, sauces, etc.	25 grams/unit	€ 10/kg	€ 0.25
Direct labor	3 minutes/unit	€ 10/hr.	€ 0.50
Total direct costs			€ 1.50
SPECIALTY SANDWICH			
Bread	1 piece/unit	€ 0.80/piece	€ 0.80
Vegetables	25 grams/unit	€ 4/kg	€ 0.10
Cheese, sauces, etc.	25 grams/unit	€ 10/kg	€ 0.25
Special ingredients	25 grams/unit	€ 20/kg	€ 0.50
Direct labor	6 minutes /unit	€ 10/hr.	€ 1.00
Total direct costs			€ 2.65

Jack knows that he should allocate all indirect costs to both types of sandwiches, but wonders why he should actually do so.

Total indirect costs are estimated to be €6,100. Total production output is 5,000 units: 4,000 regular and 1,000 specialty sandwiches. The regular sandwich has a €3 sales price; the specialty sandwich has a €4.50 sales price. A more detailed overview of indirect costs is given below.

Support function	*Amount*	*Cost Allocation Base*	*Total Cost Driver Usage*	*Usage for regular sandwiches*	*Usage for specialty sandwiches*
Administrative	€ 2,500	direct labor hours	300	200	100
Purchasing	€ 1,400	number of orders	20	12	8
Warehousing	€ 700	floor-space (m^2)	50	30	20
Marketing	€ 1,500	units sold	5,000	4,000	1,000
Total	€ 6,100				

Since indirect costs could be allocated in many different ways, Jack calculates the cost prices for both types of sandwiches using 3 methods:

1) using the number of products as a cost allocation base,
2) using the number of direct labor hours as an allocation base, and
3) using Activity Based Costing.

After applying these methods, Jack is quite confused. How can the obtained information be used to make product-mix or pricing decisions?

Literature: Bhimani et al. (MA), chapter 5 (123-131 + 139-141) and 11

Task 11 Absorption costing vs. variable costing

Because you obtained a better understanding of cost allocation (see previous tasks), it is time to start using the information about direct and indirect costs of business activities to plan and control profits.

As one of the first controlling tasks, Mr. John Cash, the controller of *Burger Queen* is occupied with planning the sales activity of frozen burgers in September 2015. The general manager, Anna Frost has also asked Mr. Cash to calculate the expected profit for the burger activity in 2015. Mr. Cash collects the relevant data.

The sales manager of BQ tells Ms. Frost that they expect to sell 500,000 burgers for €2 in 2015, which would amount to total sales of €1,000,000. The sales department also expects to have selling expenses (marketing expenses), amounting to €0.10 per burger (variable) and €50,000 (fixed), and they also tell him that they expect that there will be no inventories in the beginning of 2015. Based on these expectations, the production managers provide him with the following costs of producing 500,000 burgers in 2015:

From: Production department
To: Mr. Cash
Beginning Inventory = 0

Budgeted costs for 500,000 burgers	Costs
Direct Material (per unit)	€0.75
Direct Labour (per unit)	€0.20
Variable Manufacturing Overhead (per unit)	€0.30
Variable Marketing Costs (per unit)	€0.10
Fixed Manufacturing Overhead (total)	€210,000
Fixed Marketing Costs (total)	€50,000

A year goes by, and in January 2016 Mr. Cash is asked to calculate the actual 2015 profit. Collecting the data he finds that most of the expectations of the production and sales people were correct. The only difference between expectations and reality, however, was that production and sales were lower than expected. BQ produced 450,000 burgers, but sold 420,000 burgers instead of the expected 500,000.

Expected sales (units)	500,000
Actual sales (units)	420,000
Expected production (units)	500,000
Actual production (units)	450,000

Mr. Cash is not surprised; BQ's business is quite sensitive to general economic conditions, which could well explain the decline in sales. Nevertheless, he is glad to be able to report a satisfactory profit for 2015 to the accounting department. His assistant, Mr. Rookie, however, also does the calculations and comes up with a different result. He is much less pleased, and wonders why his calculations yield a less satisfying result. He wonders whether this might be caused by a production-volume variance. He remembers that absorption costing and variable costing can lead to different profits in a given period and wonders which method is the most appropriate to use.

Literature: Bhimani et al. (MA), chapter 7 (pp178-190)

Task 12 CVP analysis

Jane remembered learning in her marketing course that good entrepreneurs always keep an eye on their competitors. Thus, she has been looking at other sandwich bars and noticed that they all finish off bread in the oven. The sandwiches are fresher and sometimes even warm, which appeals to the customers. Back home, she does some research regarding different ovens and discusses her findings with Jack and Marie.

There are two options. Keeping new products in the future in mind, they can either buy a second-hand amateur oven for €3,600 or a new professional oven for €4,800. The new oven is more expensive, but due to new features it has the advantage of less cleaning and maintenance and it uses less energy than the second-hand oven. Compared to the basic bread, Jane expects that the new oven will create variable costs of €0.03 per sandwich and the second-hand oven of €0.09 per sandwich.

She has a quick word with their bookkeeper and he said that both machines would be depreciated straight-line in two years, as the second-hand oven is only a few months old. After two years the value is zero, so the fixed costs per year amount to 50% of the purchase price of the respective oven. For calculation purposes assume they can sell the sandwiches with fresh French bread for an additional €0.35 per sandwich to cover the cost of the oven (so they can safely ignore all other costs and revenues for the moment). They expect to sell 8,500 French bread sandwiches per year. This estimate, however, is only a guess and they also don't know how competition is going to react.

Jack and Marie agree with Jane, that selling fresh French bread might be good for their business. They decide to try and calculate which oven would be best, and calculate the break-even point for the additional income for the French bread. They decide to consult their accountant just in case.

After reading the results he makes a few calculations. Then he says: "With a production volume of 8,500 sandwiches per year we produce more than the break-even quantity. The choice of the production system depends on the trade-off between profitability and risk, and therefore on the operating leverage". He notices that they don't understand his remark and graphically illustrates the dilemma. Furthermore, he wants to provide them with some kind of sensitivity analysis relevant for their business.

Literature: Bhimani et al. (MA), chapter 8

Task 13 The Master Budget

At *Burger Queen*, Mr. John Cash has been asked to prepare the 2015 operating budget, so he starts to gather the necessary information.

The variable manufacturing costs for the hamburgers and chicken products are as follows:

	Hamburgers	Nuggets	Wings & Drumsticks
Direct labour	€ 0.20	€ 0.15	€ 0.17
Direct material	€ 0.75	€ 0.55	€ 0.57
Variable (manufacturing) overhead	€ 0.30	€ 0.25	€ 0.25

The marketing department has provided him with the following sales expectations:

- 430,000 hamburgers with a sales price of €2
- 75,000 chicken nuggets with a sales price of €1.60
- 125,000 chicken wings & drumsticks with a sales price of €1.80

From the production department Mr. Cash received the following information concerning the different products' beginning inventory:

- 15,000 hamburgers with a unit cost of €1.70
- 7,000 chicken nuggets with a unit cost of €1.40
- 11,000 chicken wings & drumsticks with a unit cost of €1.40

The desired ending inventory levels are 13,000 hamburgers, 6,000 chicken nuggets and 9,000 chicken wings & drumsticks. The company applies the FIFO method for inventory valuation.

Total fixed overhead is budgeted to be € 315,000, allocated based on the number of products. Fixed selling expenses for the entire company are estimated to be € 90,000. The variable selling expenses are expected to be € 0.10 for each product.

After collecting all the data, Mr. Spengler starts to develop the 2015 operating budget (using absorption costing).

Literature: Bhimani et al. (MA), chapter 14 (pp. 424-439)

Task 14** Wiki Art Gallery, Inc. A case for critical thinking

This instructional case requires you to provide advice to a client who is currently a co-owner of a for-profit art gallery. The client is planning to purchase his co-owner's shares at a price to be determined based on their company's recent financial performance. The company's financial statements, prepared by the client's co-owner, contain accounting choices and judgments that you should identify and evaluate using critical thinking skills.

Please prepare appendix D of the case study (questions 1-10)

The literature for this case is related to all the literature covered in the previous tasks. This requires some additional research on the Fraud triangle.

Presentation subgroup 1

Critical thinking and an introduction to accountability

This case introduces you to the accountability aspect of our course. Is everyone who is involved with accounting mistakes automatically committing fraud? How are we able to judge the decisions of our colleagues? Your task is to guide the group through the questions of the case. Make sure you address all the relevant components and questions of the task, and take ownership of the case at hand. Guide the discussion in an interactive way.

Case reference:

Phillips F., & Mackintosh B. (2011). Wiki art gallery, Inc.: A case for critical thinking. Issues In Accounting Education, 26(3), 593-608. doi:10.2308/iace-50038

Task 15** Management Control (+ case study)

Business Owners Get Burned by Sticky Fingers
The Association of Certified Fraud Examiners estimates that employee frauds at businesses with fewer than 100 employees cause a median loss of $200,000. (Source: Wall Street Journal, March 2010)

Internet misuse costs businesses $178 billion annually
Websense puts the cost at $5,000 per employee

From: **IDG News Service** July 19, 2005

Given the above headlines, it may be needless to say that the old Jewish saying "I wish you a lot of employees" is rather a cynical curse than a friendly greeting. What moves employees to engage in these acts? Finding an answer to this question brings us to the field of Management Control. Management Control addresses the question: Do employees behave appropriately?

The Management Control literature distinguishes three main reasons for not behaving in line with the objectives of the organization. First, it might be unclear to employees what is expected from them. Second, even when employees know what is expected from them, some decide not to perform in accordance with the organizational goals due to motivational problems. Third, when employees are both aware of expectations and motivated to act goal-congruent, they might still lack the necessary skills or information to perform appropriately.

Right then, that's it? Not quite! Don't you want to know what we can do about it? Ah! Might be interesting, not? Locks on doors? Cameras? Separation of duties? Computer passwords? Action accountability? Now you're talking. But guess what: these are just examples of one type of Management Control. There are two others, each of them addressing one or more of the previously mentioned problems, and each with their own pros and cons.

And what does all this have to do with accounting? The predominant control systems in most organizations are based on management accounting information, introducing the notions of responsibility centers, controllability, budgeting and financial performance target setting.

Case study about real-life Management Controls at a casino ("Controls at the Bellagio Casino Resort"). *The following issues should be addressed in the presentation:*

1. Regarding (a) key actions and (b) controls for the following casino employees: blackjack dealer, pit boss, and vice president of table games. Do you consider the controls to be tight or loose at each of these 3 levels?
2. What could go wrong at a black jack table. Do you think the controls in place are sufficient to prevent these from happening?
3. Are any of the controls in place at the Bellagio suitable for firms in other industries?

Literature:

- *Drury, chapter 11 (pp. 301-322)*
- *case study* Controls at the Bellagio Casino Resort

Presentation subgroup 2

Management Control

As mentioned in task 14, the role of management control is very important to ensure employees act in accordance with the firm's goals. However, such controls might also have harmful side effects and what does this have to do with accounting? In your presentation go beyond the topics addressed in the compulsory literature and give an interactive presentation about the role of management control. Use the case as a real-life example addressing the issues given in this task. In addition, make sure you incorporate the learning goals of task 14, but aim to involve your fellow students in the audience in answering those learning goals.

Task 16**   Auditing (+ case study)

Andrew Brown, from the United States, and Jola Czuba, from Poland, are in the international exchange program of UM's School of Business and Economics. They are both doing a major in accounting and auditing. For a class assignment, Jola and Andrew dig into the reasons for having audits in an economy. Jola, with her Eastern-European background, thinks that there are only audits because there are laws and regulations requiring companies to be audited. Andrew, who has a much more liberal attitude, thinks that all these laws and regulations are in principle not needed: there is also a strong demand for auditing without any laws and regulations: "as long as there is separation of ownership and control there will be a demand for auditors".

Obviously, Andrew and Jola have very different ideas about the regulation of auditing. However, both are convinced that society, government, business and the profession all wish to avoid future "Enrons". To this end, a wide variety of rules govern the auditor or public accountant. Andrew mentions that especially the American Sarbanes-Oxley Act has recently been a strong influence on the auditing profession.

Andrew finds an example of an auditor's report while going through the financial statements of RBK N.V., and wonders what it all means.

AUDITOR'S REPORT

INTRODUCTION
We have audited the 2012 Financial Statements of RBK N.V.. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these Financial Statements based on our audit.

SCOPE
We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Financial Statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the Financial Statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

OPINION
In our opinion, the Financial Statements give a true and fair view of the financial position of the company as at December 31, 2012 and of the result for the year then ended in accordance with International Financial Reporting Standards.

Maastricht, February 22, 2013

For MIAMU Accountants

L. Timmermans RA   H.F.D. Hassink RA

Case study about a real-life auditing decision: "Ocean Manufacturing Inc. – The New Client Acceptance Decision". *The following issues should be addressed in the presentation:*

1. The procedures an auditor should perform in determining whether or not to accept (or retain) a client.
2. Using Ocean's financial information, perform preliminary analytical procedures (that is, calculate relevant ratios) to obtain a better understanding of the prospective client and to determine how Ocean is doing financially. Compare Ocean's ratios to the industry ratios provided. Discuss any major differences and concerns that arise from this analysis.
3. What non-financial matters should be considered before accepting Ocean as a client? How important are these issues to the client acceptance decision, and why?
4. Would you recommend accepting Ocean as an audit client? Carefully consider both positive and negative factors, and include both financial and non-financial issues.

Literature: Knechel, chapter 1, 2 (pp. 27-29), 3 (pp. 72-77), and 4 (pp.111-122)

Presentation subgroup 3

Auditing

What is de purpose of auditing? Does it have the desired effect; avoiding future "Enrons"? How come the American Sarbanes-Oxley Act has a strong influence on the auditing profession? In your presentation go beyond the topics addressed in the compulsory literature and give an interactive presentation about Auditing. Use the case as a real-life example addressing the issues given in this task. In addition, make sure you incorporate the learning goals of task 15, but aim to involve your fellow students in the audience in answering those learning goals.

Task 17** Corporate governance

Corporate governance has become one of the most commonly used concepts in the current global business vocabulary. The notorious collapse of Enron in 2001, one of America's largest companies, has focused international attention on company failures and the role that strong corporate governance needs to play to prevent them. Especially the American Sarbanes–Oxley Act of 2002 has had an enormous impact. Nations around the world are instigating corporate governance reforms, as evidenced by the proliferation of corporate governance codes worldwide.

Despite, and perhaps because of, all these dispersed efforts to improve corporate governance there is no single, accepted definition of what actually constitutes corporate governance. Furthermore, the subject may be treated in a narrow or a broad manner, depending on the viewpoint of the policy maker, practitioner, researcher or theorist. It seems that existing definitions of corporate governance fall along a spectrum, with 'narrow' views at one end and more inclusive, 'broad' views placed at the other.

Most economists would simply state that it should be maximization of the long-term market value of the firm. This so-called value maximization – or shareholder theory – proposition has its roots in 200 years of research in economics and finance. This point of view is especially attributed to Milton Friedman in his famous article *The social responsibility of business is to increase its profits* (NY Times, 1970), in which he essentially states that "the business of business is business". This however, does not paint the complete picture of Friedman's thoughts on the social responsibilities of business.

The main contender to value maximization as the corporate objective is called stakeholder theory. In contrast to the grounding of value maximization in economics, stakeholder theory has its roots in (amongst others) sociology. It focuses not only on financial performance, but also on the wider social responsibilities of business. Stakeholder theory is now popular and has received the formal endorsement of many professional organizations, special interest groups, and governmental bodies.

Required literature:

- Friedman, M. (1970). *The social responsibility of business is to increase its profits*. The New York Times Magazine, September 13th.
- Kim, Nofsinger & Mohr, chapter 1, 2 and 4.
- Smith, H.J. (2003). *The shareholder vs. stakeholder debate*. MIT Sloan Management Review, summer 2003, p.85-90.

Additional literature (not required):

- Kim, Nofsinger & Mohr, chapter 10: *Moral hazard, systemic risk, and bailouts*[4]

Presentation subgroup 4

Corporate Governance: History, Components and Recent Developments

As mentioned in task 16, the field of corporate governance can be interpreted as covering a very broad spectrum of topics. It can be viewed as covering all or some of the following (and this is not an exhaustive list): the principal-agent conflict, monitoring by the board of directors, executive compensation, shareholder rights, threats of takeover, accounting & auditing, corporate social responsibility, and regulation. Furthermore, differences exist between governance structures and regulation worldwide.

In your presentation go beyond the topics addressed in the compulsory literature and give an <u>interactive</u> presentation about what you consider to be important topics in

[4] In chapter 10, Kim et al. discuss the role of (flawed) corporate governance in the recent financial crisis.

corporate governance. In doing so, incorporate the learning goals of task 16, but make sure you involve your fellow students in the audience in answering those learning goals.

Task 18** Accounting Fraud & Corporate Governance: WorldCom case

In this tutorial meeting we will discuss a case study of one the most famous accounting frauds of the last decade: WorldCom. In order to engage in a meaningful discussion, every student has to thoroughly prepare the case and – in advance (!) – answer the following questions:

1. What are the pressures that lead executives and managers to *cook the books*?
2. What is the boundary between earnings smoothing or earnings management, and fraudulent reporting?
3. Why were the actions taken by WorldCom managers not detected earlier? In your analysis, consider at least the following 4 factors:
    a. Leadership and corporate culture
    b. Internal control & audit
    c. External auditor (Arthur Andersen)
    d. Board of directors
4. Betty Vinson: victim or villain? Should criminal fraud charges have been brought against her? How should employees react when ordered by their employer to do something they do not believe in or feel uncomfortable doing?

Presentation subgroup 5

Accounting Fraud at WorldCom

During this meeting one of the subgroups is responsible for facilitating an in-depth discussion of the case. In order to achieve this, the subgroup has to give an interactive presentation including a short introduction to the case and acting as discussion leaders in the discussion of the abovementioned case questions. Incorporating additional information into the presentation is highly advisable.

Appendix 1 Presentation evaluation form

PRESENTATION EVALUATION FORM

Topic of the presentation:

Names of the speakers:

Name of the observer:

A. Evaluate the presentation by answering the following general questions:
1. In general, what did I like about the speakers?

2. In general, what could the speakers improve?

B. Please indicate the quality of the presentation on basis of the following criteria.
1 = very bad; 2 = insufficient; 3 = sufficient; 4 = good; 5 = very good

INTRODUCTION	
The opening of the presentation catches the interest of the audience	1 2 3 4 5
The purpose and structure of the presentation is clarified	1 2 3 4 5
STRUCTURE OF THE PRESENTATION	
There is a clear distinction between introduction, body and conclusion	1 2 3 4 5
The main points of the presentation are clear	1 2 3 4 5
APPEARANCE AND DELIVERY	
The presentation is free from reading	1 2 3 4 5
The speaker is aware of the audience	1 2 3 4 5
Overall, the presentation style is engaging	1 2 3 4 5
CONTENT OF THE PRESENTATION	
The presentation discusses the topic in a systematic manner	1 2 3 4 5
The presentation contains links to (literature used in) other sessions	1 2 3 4 5
The presentation integrates the different pieces of literature	1 2 3 4 5
The speaker helps the audience understand important concepts/ideas	1 2 3 4 5
The speaker involves the audience (e.g. by asking questions)	1 2 3 4 5
The presentation includes additional literature or other resources	1 2 3 4 5
The presentation provides challenging discussion points	1 2 3 4 5
Questions are answered adequately	1 2 3 4 5
USE OF VISUAL AIDS	
The slides are readable and clear	1 2 3 4 5
The slides are effectively used to aid clarity and heighten impact	1 2 3 4 5

FINAL ASSESSMENT OF THE PRESENTATION 1 2 3 4 5 6 7 8 9 10