

## Case 5 - Receivables and Reserves

The following case relates to United Continental Holdings, Inc., an airliner.

### Schedule II

#### Valuation and Qualifying Accounts For the Years Ended December 31, 2015, 2014 and 2013

<u>(In millions)</u>	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions (a)	Other	Balance at End of Period
<u>Description</u>					
Allowance for doubtful accounts—UAL and United:					
2015	\$ 22	\$ 25	\$ 29	\$ —	\$ 18
2014	13	45	36	—	22
2013	13	35	35	—	13
Obsolescence allowance—spare parts—UAL and United:					
2015	\$ 169	\$ 38	\$ —	\$ 28	\$ 235
2014	162	35	28	—	169
2013	125	38	1	—	162

Using the above table, please answer the following questions (**Please ignore other**).

1. What was the amount of United's bad debt expense for 2015?

**\$25**

2. What was the amount of receivables written-off, net of recoveries, during 2015?

**\$29**

3. What effect did the write-offs have on net income and on ending total assets for 2015?

**No effect on net income**

**No effect on total assets**

4. What is the effect of recognizing a bad debt expense on the firm's 2015 cash flows from operations?

**No effect**

5. Regarding the obsolescence allowance:

- a. What was the amount of parts expense for 2015?

**\$38**

- b. What was the amount of parts actually going obsolete during 2015?

**\$0**

Excerpts from United (UAL) 10-K for the year ended December 31, 2015 are presented below. Please use them to answer the following questions.

6. Assume that all passenger revenue flow through either accounts receivable or frequent flyer deferred revenue and advanced purchase of miles. Estimate the cash collected from customers using data from the cash flow and income statements. Hint: think whether you should include in your answer advanced ticket sales.

$$32785 - 200 + 52 - 15 = 32622$$

7. By how much would United's 2015 net revenues change if, throughout its history, it had been recognizing frequent flyer deferred revenue and advanced purchase of miles from customers as revenues (rather than deferring)?

$$2117 - 2058 + 2826 - 2879 + 1010 - 1217 = -201$$

**Net revenues will decrease by 201**

8. Explain why United would be violating U.S. GAAP if it recognized revenue at the time advances were received from customers.

**By the matching principle, when revenues are recognized, all expenses current and future need to be recognized in the income statement.  
The risks have not been transferred.**

UNITED CONTINENTAL HOLDINGS, INC.  
CONSOLIDATED BALANCE SHEETS  
(In millions, except shares)

	At December 31,	
LIABILITIES AND STOCKHOLDERS' EQUITY	2015	2014
Current liabilities:		
Advance ticket sales	\$ 3,753	\$ 3,701
Frequent flyer deferred revenue	2,117	2,058
Accounts payable	1,869	1,882
Accrued salaries and benefits	2,350	1,818
Current maturities of long-term debt	1,224	1,313
Current maturities of capital leases	135	110
Fuel derivative instruments	124	694
Other	842	932
	<u>12,414</u>	<u>12,508</u>
Long-term debt	9,673	9,953
Long-term obligations under capital leases	727	571
Other liabilities and deferred credits:		
Frequent flyer deferred revenue	2,826	2,879
Postretirement benefit liability	1,882	1,933
Pension liability	1,488	2,226
Advanced purchase of miles	1,010	1,217
Deferred income taxes	—	1,000
Lease fair value adjustment, net	359	466
Other	1,516	1,446
	<u>9,081</u>	<u>11,167</u>

UNITED CONTINENTAL HOLDINGS, INC.  
STATEMENTS OF CONSOLIDATED CASH FLOWS  
(In millions)

	Year Ended December 31,		
	2015	2014	2013
Cash Flows from Operating Activities:			
Net income	\$ 7,340	\$ 1,132	\$ 571
Adjustments to reconcile net income to net cash provided by operating activities -			
Deferred income taxes	(3,177)	13	(14)
Depreciation and amortization	1,819	1,679	1,689
Special charges, non-cash portion	247	78	50
Other operating activities	115	(21)	18
Changes in operating assets and liabilities -			
(Increase) decrease in fuel hedge collateral	551	(577)	—
Unrealized (gain) loss on fuel derivatives	(305)	436	(56)
Decrease in other liabilities	(198)	(238)	(201)
Decrease in frequent flyer deferred revenue and advanced purchase of miles	(200)	(88)	(415)
(Increase) decrease in other assets	(160)	(34)	164
Decrease in accounts payable	(77)	(251)	(265)
Increase in advance ticket sales	52	296	45
(Increase) decrease in receivables	(15)	209	(142)
Net cash provided by operating activities	5,992	2,634	1,444

**UNITED CONTINENTAL HOLDINGS, INC.**  
**STATEMENTS OF CONSOLIDATED OPERATIONS**  
(In millions, except per share amounts)

	Year Ended December 31,		
	2015	2014	2013
Operating revenue:			
Passenger—Mainline	\$ 26,333	\$ 26,785	\$ 25,997
Passenger—Regional	6,452	6,977	7,125
Total passenger revenue	32,785	33,762	33,122
Cargo	937	938	882
Other operating revenue	4,142	4,201	4,275
	<u>37,864</u>	<u>38,901</u>	<u>38,279</u>