

# The Professional's Playbook: How to Crack a 10-K Report

A structured, expert-level framework for analyzing a 10-K report to identify business health, risks, and financial red flags.



## PASS 1: RECONNAISSANCE (THE 30,000-FOOT VIEW)

Initial Scan for Strategic Positioning & Major Threats (15 mins)



## PASS 2: THE DEEP DIVE (MANAGEMENT & MARGINS)

Scrutinize Narrative, Performance Trends & Tone Changes



## PASS 3: FORENSIC ACCOUNTING (THE FOOTNOTE DETECTIVE)

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Dig into Footnotes for Hidden Landmines & Creative Accounting

### QUICK CHECKPOINTS

Risks Business Overview

Annual Report 10-K SEC EDGAR

Glossy Annual Report

Item 1: Business. Assess customer concentration, market position, and core operations.  
Item 1A: Risk Factors. Identify what keeps management awake at night, with alert red for significant competitive or debt risks.

### NARRATIVE VS. NUMBERS ANALYSIS

Item 7: MD&A (Management's Discussion & Analysis). This is the "editorial" section. Compare management's narrative explanation with results and future plans against Item 6 (Financial Data) trends.  
Tone Check: Watch for subtle shifts in language from previous years, signaling potential hidden concerns.

### RED FLAG ALERT SYSTEM

Item 8: Financial Statements & Supplementary Data. Dig into footnotes (the core audited data) for:

- Pending lawsuits and regulatory investigations (Commitments & Contingencies).
- Aggressive revenue recognition policies.
- Excessive stock-based compensation.

Item 9: The Red Flag Section. Discloses disagreements with accountants; changes in accounting firms are a major warning sign.

### THE PROFIT VS. CASH GAP & FORENSIC CHECKS



START WITH:  
Net Income  
(Accrual Basis)

+

ADD BACK:  
Non-cash items  
(e.g., Depreciation, Stock-Based Compensation)

=

OPERATING  
CASH FLOW  
(Cash Basis)

STATISTIC: AI research indicates "Financial Profile" features (debt, equity, taxes) are strongest predictors of future profitability over simple ratios.

### FORENSIC CHECKLIST & RED FLAGS

- Revenue Recognition Policy: Check how the company "books" sales; aggressive policies inflate revenue before cash is collected.
- Commitments & Contingencies: Buried in footnotes, detailing pending lawsuits or regulatory actions that could wipe out future profits.
- Auditor's Opinion: Look for "Unqualified Opinion" (Standard), "Qualified" or "Disclaimer" opinions are urgent signals to investigate.

### ESSENTIAL LIQUIDITY AND PROFITABILITY RATIOS FOR 10-K ANALYSIS

Ratio Category	Key Formula	Interpretation
Liquidity	Current Ratio (Current Assets / Current Liabilities)	Ability to meet short-term obligations (Target > 2)
Profitability	ROE (Net Income / Avg. Shareholders' Equity)	Efficiency of using shareholder money to generate profit
Solvency	Debt to Assets (Total Debt / Total Assets)	Percentage of assets financed by creditors vs. owners
Efficiency	Inventory Turnover (COGS / Avg. inventory)	How many times a company sells and replaces inventory in a year