

E5-1 If purchased goodwill is not amortized, amortization expense will be less, net income will be greater, assets and equity will be greater than if the change had not been implemented.

E5-2 a. The increase in inventories means that Cisco was producing or purchasing more inventories than it could sell, if the inventory increase could not be justified by the increased sales. The fact that receivables grew faster than sales can be attributed to significant sales right at the end of the fiscal period, a change in the type of customers to less credit worthy customers or a slow down in payments from customers for other reasons such as dissatisfaction with the product.

b. Financial analysts were concerned for a number of reasons:

1. Growing inventories relative to sales will mean that Cisco may have to reduce selling prices, cutting into profit margins.
2. Large customers are ordering fewer goods, hurting future revenues. For example, sales to auto makers were projected to be \$100 million less than what the company had predicted only a few months previously.
3. Many smaller customers that have provided a base for future growth have gone out of business or downsized significantly. In fact sales to dot-coms fell to half of the previous year's levels.
4. The change in accounts receivable relative to sales suggested that the sales force struggled to record sales in the closing days of the quarter. This would suggest even slower revenue growth in future quarters.

E5-3 a. According to the Financial Accounting Standards Board's Statement of Financial Accounting Concepts Number 5, revenue should not be recognized until it is realized or realizable and earned. In Staff Accounting Bulletin 101, the SEC reiterates FASB's criteria, stating that revenue is generally realized or realizable and earned when: 1) persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the seller's price to the buyer is fixed or determinable and collectibility is reasonably assured. The SEC's interpretive response regarding layaway sales states that, provided that the other criteria are met, revenue from sales made under a layaway program should be recognized upon the delivery of the merchandise to the customer. The justification is that, generally, the selling company retains the rights of ownership of the merchandise, receives only a deposit from customers, and does not have an enforceable right to the remainder of any purchase price. (SEC Staff Accounting Bulletin 101)

b. Income, assets, and equity would decrease in the period of the change. Liabilities would increase.

c. The deferral would require TJX to reduce sales in the period of the change was made. On the income statement, sales and cost of goods sold would decrease. On the balance sheet, accounts receivable would decrease and inventories would increase. Any deposits received on the layaway merchandise result in an increase in unearned revenue. The SEC suggests the caption "deposits received from customers for layaway sales." Retained earnings would decrease as a result of the accounting change.

E5-4 Income can decline because the company can be recognizing significant expenses that do not affect cash in the period the expenses were recognized or that are noncash expenses that will never affect cash. In Viacom's case, the company recognized a drop in the value of its Internet investments. This recognition required the company to take a charge to earnings while reducing the value of the Internet investments on its balance sheet. This is a "noncash" adjustment that does not affect cash flow. In addition, the company's results reflected higher amortization of goodwill, resulting from Viacom's merger with CBS. Amortization of goodwill is a noncash expense. The company's cash flow (earnings before interest, taxes, depreciation and amortization), increased from \$595 million the year earlier to \$1.36 billion.

E5-5

Transaction	Revenues	Expenses	Income	Assets	Liabilities	Equities
b.	NE	NE	NE	+	+	NE
c.	NE	NE	NE	NE	NE	NE
d.	NE	+	-	-	NE	-
e.	NE	+	-	-	NE	-
f.	NE	NE	NE	+	+	NE
g.	+	+	+	+	NC	+
h.	NE	+	-	-	NE	-
i.	+	NE	+	NE	-	+
j.	NE	+	-	-	NE	-
k.	NE	+	-	NE	+	-
l.	NE	+	-	NE	+	-
m.	NE	+	-	NE	+	-

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Transaction	Revenues	Expenses	Income	Assets	Liabilities	Equities
b.	NE	U	O	O	NE	O
c.	NE	U	O	O	NE	O
d.	U	NE	U	U	NE	U
e.	U	NE	U	NE	O	U
f.	NE	U	O	O	NE	O
g.	NE	NE	NE	U	U	NE
h.	NE	U	O	NE	U	O
i.	NE	U	O	O	NE	O
j.	O	NE	O	O	NE	O