Spring 5-7-2022

Practicum in the Study of Financial Accounting

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PRACTICUM IN THE STUDY OF FINANCIAL ACCOUNTING

by

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A thesis submitted to the faculty of The University of Mississippi in partial fulfillment of the requirements of the Sally McDonnell Barksdale Honors College.

Oxford

May 2022

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ABSTRACT:

This paper was intended to be a practicum in the study of financial accounting. The different sections encompass many distinct aspects of the field and was completed over two semesters. Each section had a goal to investigate a specific area related to accounting, and my mission was to focus on this area and express my thoughts on the section. To do this, I would explain how each topic was related to accounting and how that would affect me in my future positions – often alone but sometimes as a part of a group. Additionally, this deep dive into the various aspects of accounting culminated in a project where our groups used their knowledge to complete a tax assessment, an audit, and an advisory engagement on a publicly traded company. As a group, we then turned this into a presentation and expressed our opinions to a panel of industry professionals and professors. Overall, this practicum allowed me to have a deeper understanding of the field in which I hope to practice in the future and opened my eyes to the many distinct aspects of the real world that relate to accounting.

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I - A COMPARISON OF POTENTIAL HOME CITIES:
SEATTLE, WA, AND MEMPHIS TN

Introduction:

For this case, our objective was to select the top two cities we are interested in interning in and working in after graduation and compare them to each other and to the places we have lived before. We were given a set of questions to answer to help guide us through learning about the cities we chose, cities we may have never even been. The questions were meant to go deeper than the surface level questions people want to know about a city and explore what life in the city is actually like, details that most people never think about until it's too late. This all helped achieve the ultimate goals of determining if we would enjoy working and living in the cities we chose and deciding which one is the best fit for us.

While doing my research for this case, I uncovered many things that I had not previously considered. The first of the surprising facts was just how big both cities were. I knew they were both fairly large, but considering the metro areas, they were both more populous than I had expected. The next was the difference in the costs of living. I knew going in that Seattle was going to be the more expensive city, but the main difference in the cities was certainly the quality and cost of apartments. For Memphis, there were a list of suitable apartments well within my budget that were in great locations. Seattle on the other hand, it took a great deal more searching just to find something reasonably within my budget. Only a handful of those within my budget were within a reasonable commute to the area I expect to work and even fewer of those were large enough. This let me know that if I were to accept a job in that area, I should probably learn to adjust to either a commute or a smaller living space. By far the most shocking detail I found in my searching was the travel times. This is something I should have considered before, but I greatly underestimated the flight time home from Seattle. Overall, I think this was a great exercise to get us to consider various aspects of where we want to live after graduation, and it certainly raised a lot of good questions that I need to answer in the next two years.

What is the population?

According to the data from censusreporter.org, Memphis and Seattle have a population of six hundred and fifty thousand and seven hundred and fifty thousand people, respectively. Though this does not seem like an enormous difference, when you consider the metropolitan areas of each city, the Memphis area is home to 1,350,000 people and Seattle includes near 4,000,000, making it the more urban of the two. While I have no previous experience living in a city this large, I find this range in population appealing. These larger populations will give me more opportunities to start and grow my career without having the overwhelming size and population of massive cities such as New York or Los Angeles. Additionally, the cities are social and cultural hubs in their own right, which is something I have always longed for growing up in rural Mississippi. Because of its larger population, I believe Seattle to be a better fit for me in this regard.

Describe the climate and seasonal fluctuations. Are you accustomed to living in this weather? If not, describe some of the challenges from this climate.

On average, the climate of Memphis is remarkably similar to the climate of my hometown. It has hot and extremely humid summers that drag on forever, mild if not slightly warm spring and fall seasons, and cool winters where the temperature rarely drops below freezing. The main difference in the climate I grew up in and the climate in Memphis is the fact that it rains drastically more in the winter in Memphis, but that is something I've gotten used to during my time living in Oxford. Seattle, on the other hand, is a vastly different climate. The temperatures are lower all year than I am accustomed to. For me, this is an important thing. Having summer temperatures being in the seventies instead of the nineties sounds delightful, and the increase chance of snowfall in the winter would be a pleasant change. The downfall of Seattle's climate is its notorious rainy days. I want to have so many cloudy and rainy days would become dreary which is why I believe Memphis has a slight advantage when it comes to climate.

Describe the city's topography, scenery, and other geographic or geological features of the area in which the city is located. Include pictures where appropriate.

Memphis is situated on the banks of the Mississippi river. The area itself is relatively flat and surrounded by pine forest. There are few other geological features but being on the river always elevates the scenery and makes the skyline of the city that much more dramatic, especially at sunset.

1. *Big Cypress Balcony* Source: Basspro.com

On the other hand, Seattle is a relatively hilly city located on the Puget sound. Being situated between the Olympic mountains and the Cascade Range makes for stunning views from the city, especially in the fall and spring. Additionally, there are three national parks and a host of other state parks within driving distance, encompassing some of the most stunning scenery and geological features in the US including lakes, glaciers, and volcanoes. Inside the city itself are numerous parks, and a skyline made famous by the Space Needle, making Seattle the easy winner when it comes to scenery and geographical features.

2. *Seattle Skyline view from Queen Ann Hill* Photographer Daniel Schwen

<u>What are the individual tax rates within the city (e.g., consider federal, state, and local income tax, property tax, and any other taxes you would be likely to pay? Quantify what this means based on a starting salary of approximately $55,000/year)?</u>

*Chart is for single filers making $55,000 per year based on IRS.GOV, dor.wa.gov, and tn.gov data

Tax	**Seattle**	**Memphis**
Federal income tax:	22% marginal tax rate, 9.59% effective tax rate	22% marginal tax rate, 9.59% effective tax rate
State tax:	6.5% state sales tax	7% state sales tax
Local tax:	10.1% total sales tax meaning 3.6% comes from local sales taxes	9.75% total sales tax meaning 2.75% comes from local sales tax
Property tax;	Average effective property tax of 0.95%	Average effective property tax of 1.472%
Other taxes:	Sweetened beverage tax of $0.0175 per ounce	6% tax on interest and dividends

Figure 1

Using the calculation tool on Smartasset.com, my total estimated tax burden for living in Memphis or Seattle is $14,891 and $13,710, respectively. The majority of this expense is due to federal income tax which is the same for both cities. The two cities are comparable when it comes to total sales tax (10.1 percent for Seattle, 9.75 percent for Memphis). The difference arises mostly from property tax with Shelby County (Memphis) being a bit higher than King County (Seattle). This difference could actually be non-existent if I choose to rent. The sweetened beverage tax in Seattle should not make much of a difference as I do not drink that much soda, but the six percent tax on interest and dividends could possibly affect my taxes. This probably will be a non-issue early on, but as I start to make more money it could add up.

What transportation hubs are in the city?

Both Memphis and Seattle have large and accessible transportations hubs within the city. Because of the FedEx shipping hub, Memphis International airport is the busiest cargo airport in the country, with daily flights to all corners of the world. According to research done by WalletHub, the public transportation in Memphis, which includes both buses and a trolley system is surprisingly great with high marks for reliability (McCann). According to the same study, public transportation is Seattle is the best in the country. From busses, to monorails, to ferries the vast and dependable transportation makes traveling the city a breeze. That added to the second largest seaport and eighth busiest airport in the country make Seattle a wonderful place to commute locally, domestically, and internationally.

What is the city's most prevalent industries? What is this city's five largest companies?

The industries in Memphis and Seattle are both remarkably diverse. Industry in Memphis is largely focused on sectors like agribusiness, advanced manufacturing, and transportation and Logistics. The city is home to three *Fortune* 500 companies – FedEx, AutoZone, and International Paper—as well as a myriad of other large companies such as ServiceMaster and Mueller Industries. Comparatively, the industry in Seattle is focused largely on technology and advanced manufacturing. Some of the largest and most well-known companies in the country, if not the world, are based in Seattle and the surrounding area including Costco, Amazon, Microsoft, Starbucks, Paccar, and Nordstrom.

Describe the quality of the city's healthcare. Describe the quality of the city's school districts (K-12). Would your children attend public or private school?

When it comes to healthcare, Seattle and Memphis could not be more different. Seattle is consistently known as one of the healthiest cities in the country while Memphis is on the other end of the spectrum, mired down by obesity and its effects like so many other cities in the south. According to another WalletHub study, Seattle is ranked second in "healthiest places to live" scoring consistently high for health care, food, fitness, and green space. Memphis is one hundred and seventieth (McCann).

Like most cities, Memphis and Seattle have a wide range in the quality of their schools, but both cities have highly rated public-school systems. Each city host some of the best schools in their respective states, but Seattle has a slight advantage in this aspect because Washington State's school system is a bit better than that of Tennessee. Also, if you consider the surrounding metro area, Seattle contains some of the best schools in the U.S. This is especially important because my partner and I are proponents of public education, so our children will certainly attend public schools.

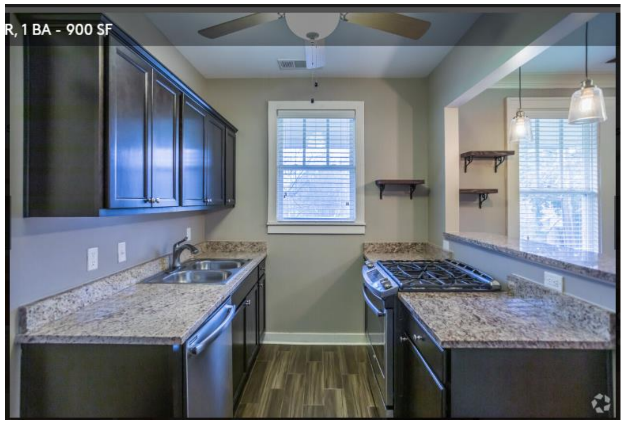
What types of crime are common within the city and where are the locations within the city to avoid?

The city of Memphis has long been known as one of the most dangerous cities in America. In almost every crime statistic imaginable (violent crime, assault, robbery etc.), Memphis is substantially higher than the national averages. On the bright side, this crime is mostly concentrated in just a few areas of the city: Downtown, Parkway Village, and Shelby Forest-Frayser. Most of the rest of the city's neighborhood crime rates are at or below national averages. As for Seattle, the city as a whole has above average crime rates, and property crimes are more common than in most other large cities. Like Memphis, crime in Seattle is highly concentrated in districts like Belltown, First Hill, South Lake Union, and Atlantic, leaving the majority of the city safe and relatively crime free.

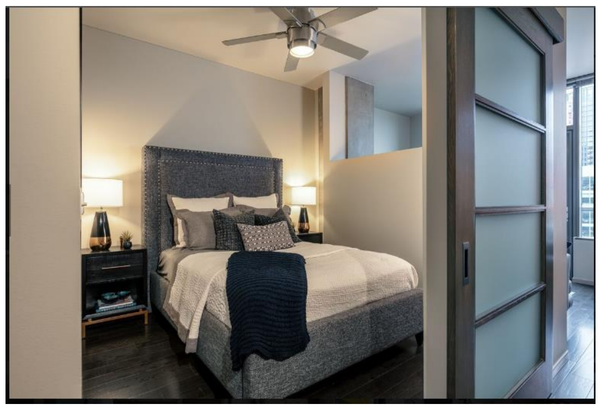
Based on where you see yourself living for the first three years, how much rent do you expect to pay? Back up this assertion with sample properties from each location (including pictures). Describe the square footage, amenities, need for a roommate, availability of parking, etc.

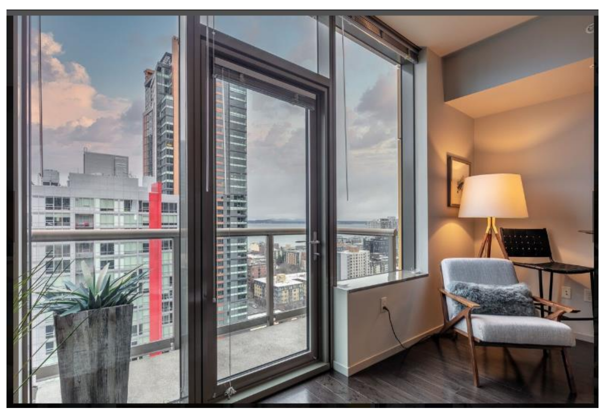
*Assuming $1,500 per month max rent budget – 30 percent of $60,000 yearly income ($5,000 monthly)

In Memphis, this $1,500 goes much further than in Seattle. For only $1,349 per month, I can rent a nice, nine hundred square foot apartment in the middle of midtown, one of the most popular neighborhoods in the city all without the need for a roommate. The apartment includes additional storage spaces, a remodeled kitchen, hardwood floors, as well as a parking spot and a list of other amenities.



In Seattle, having a roommate would save money, but I would not have to have one. For $1,470 per month, I could get a five hundred seventy-five square foot, one-bedroom apartment near downtown. With this comes a modern kitchen, outdoor patio area, bike storage, and a fitness center. Parking is available onsite, but there is a fee.





What is the typical mode of commuting? Based on your answers identified in the prior question, what are your likely commute times?

Because Memphis is such a drivable city, the most typical mode of commuting would be driving a personal vehicle. Due to the convenient location of the apartments in the Memphis area that I found; the commute time should only be around twenty minutes.

In Seattle, on the other hand, public transportation such as busses and the monorail are the main form of transport. The superb transit in the city means that my commute time, if I take the bus, would be between ten and fifteen minutes. Also, if the notoriously rainy weather permits, I could walk to most places in twenty minutes and bike there in ten.

Where will you do your grocery shopping?

For the apartment I chose in Memphis, I have a lot of options for grocery shopping. There is a Kroeger less than a mile down the street. because it is so easy to drive in the city, I could easily drive to stores such as Whole Foods or Costco in just a short time. In Seattle, shopping is a bit more difficult because I would not be able to drive. Luckily, within half a mile from the apartment I found is a Whole Foods as well as an Amazon Go market.

How will you do your laundry?

Luckily enough, the apartments I found in both cities had a washer and dryer included in the apartment. This seemed to be the norm from what I saw in my searching, and at a minimum, there was a place to do laundry in the building. If washer and dryers had not been included, though, I think I would rather find a roommate and get a nicer place. The inconvenience of having to take my laundry somewhere is a deal breaker for me.

Name at least three civic, religious, or charitable organizations you would like to be active in for each city?

Volunteering my spare time to charitable organizations is something that is especially important to me, so I was glad to see so many wonderful opportunities. In both cities, there are a plethora of soup kitchens, food pantries, and animal rescues that I would love to serve, but there are also opportunities at larger organizations. Both St. Jude's Children's Research Hospital and Ducks Unlimited's wetland conservation are centered in Memphis, and it would be profoundly satisfying to help in any capacity. In Seattle, the Islandwood organization that educates children on the environment as well as the Bill and Melissa Gates foundation, one of my favorite charities, would be opportunities to give back.

<u>What are the sports, entertainment, or recreational activities that you would be most likely to engage in within the city? Name at least five activities.</u>

Memphis is well known for its blues and barbeque joint, so it is a wonderful place for live music, food, and festivals at almost any time. The Memphis Theatre is also pretty great by all accounts. Additionally, the Memphis Grizzlies and Redbirds provide plenty of opportunities for watching sports, and the city is within driving distance of a number of great fishing, kayaking, and camping locations. As for Seattle, there are a host of professional sports like the Seattle Mariners, the upcoming NHL team the Seattle Kraken, as well as the Seattle Seahawks at their legendary CenturyLink Field. The city is also known for its theatre, art festivals, and nineties grunge music of which I am so fond. Finally, Seattle is located right in the middle of some of the best hiking and camping sites in the country and is home to a famously tasty food and craft beer scene.

<u>What are the modes of traveling back to your hometown from this city? What is the average cost you would incur for each trip back home? How long will it take to reach your home?</u>

Travelling home, would be a breeze from Memphis. It is only a five-and-a-half-hour drive, which is only a little longer than my drive home now. It is around three hundred and fifty miles, so assuming thirty miles per gallon and two dollar per gallon gas, I could make the trip home and back for less than fifty dollars. Seattle is a different story; the forty-hour drive is a little daunting. The best option is a flight into the Mobile airport, which is still an hour from my hometown. In total, the trip would take nearly ten hours one way and cost nearly four hundred dollars.

<u>Based on your findings, develop a model monthly operating budget for each city for Year 2, assuming that with bonuses for being a high performer, your annual salary is $60,000.</u>

	<u>Memphis:</u>	**<u>Seattle:</u>**
<u>Rent:</u> (From above)	$1,349	$1,470
<u>Transportation:</u> (Car in Memphis, public transportation and ride shared in Seattle)	$600	$500

<u>Insurance:</u> (Best estimates)	$500	$500
<u>Food:</u> (Best estimates)	$450	$550
<u>Entertainment:</u> (Best estimates)	$200	$200
<u>Utilities:</u> (Rounded: data from google search)	$200	$200
<u>Taxes:</u> (From above)	$1,241	$1,143
<u>Savings:</u> (Flexible - just what was left over from other calculations)	$460	$337

Figure 2 *Per month Basis ($60,000 per year = $5,000 per month)

<u>Finally, based on your full analysis, determine which one is your preferred city and why?</u>

Based on the full analysis provided above, I prefer Seattle over Memphis. I think it is a wonderful city with great opportunities for jobs, entertainment, and a productive future. That being said, the fact that the cost of living is higher and being so far away from my current home makes it a much closer competition. In the end, Memphis is also a lovely city and I think where I will ultimately end up will come down to the offers that I may receive.

II - CONTEMPLATION OF ASSET CONCEPTS

Completed by a group consisting of Mary Grace Gaines, Laine Keel, Olivia Meyer, and Kate Sudduth

Introduction:

For case two, we were assigned to work as a group to discuss a preselected set of dimensions regarding certain aspects of asset accounting. For the sake of the case, our group had to assume that we were members of the Financial Accounting Standards Board (FASB) and decide between the evaluation standards presented. In the beginning, we found it difficult to reimagine the fundamental accounting concepts that we have studied in order to accommodate these new viewpoints. However, this case allowed us to advance our understanding of asset accounting.

The first question asked us to decide whether the valuation of assets and liabilities or the determination of expenses and revenues was the primary goal of financial reporting. It seemed like both were integral parts of the accounting process; however, when forced to choose just one to be the main focus of determining new accounting standards for the FASB, viewpoint two made the most sense. As you will read, our thought process centered around the idea that revenues and expenses best display a company's success. Making sure that a company's profitability is completely transparent seemed the most important because of the fact that financial reporting is for external users.

The second question asked us to consider whether assets should be measured as "value in exchange" or "value in use." As a group we struggled more with this question conceptually. Ultimately, we decided that assets realize their contribution to a firm by being consumed in combination with other assets. This creates firm-specific value proportionally to the assets' exchange value. Recognizing firm-specific value over the life of the asset rather than just the market value at the time of sale seemed more relevant in our opinion.

Finally, the third question asked us how accounting for assets would change based on the viewpoint we favored in the previous question. Our group designed journal entries around the concept of a "Firm-Specific Value" account that would show up on the balance sheet. This "asset" would be created at the time of purchase and depreciate the same way any asset would. This idea is very far-fetched and maybe not implementable, but we tried to think creatively about this assignment.

Ultimately our understanding of asset accounting was challenged throughout the duration of this case. Not everything we discussed always made sense, but we think we were successful at thoughtfully finding pros and cons for each viewpoint presented. We are excited to see how the future of accounting continues to advance as financial reporting for assets and liabilities changes.

Question 1: **Read and consider the following two viewpoints. Discuss which viewpoint should be the FASB's focus when promulgating new standards. Take excellent notes of your group's discussion and write a fully developed brief**

highlighting the pros and cons of each viewpoint culminating with a final decision based on the consensus of your group. Explain why that viewpoint won the debate.

Olivia: “Okay, so let’s start with viewpoint one. What did everyone take from it?”

Kate: “I don’t necessarily agree with viewpoint one more than viewpoint two, however, I think that viewpoint one is more useful to internal users instead of external users.”

Olivia: “I agree, since evaluating the assets and liabilities of the company is not going to be as beneficial for financial reporting as it would for managerial purposes.”

Kate: “I also think that unrealized gains and losses are subject to change and do not necessarily reflect the success of a firm or company.”

Laine: “I think it could reflect the success of some companies who focus on bringing in a large number of assets like a bank or an investment firm.”

Olivia: “Those are really the only type of institutions I can see this working for.”

Mary Grace: “Going off that, viewpoint one might offer some false promises because assets may be profitable, but if there are large amounts of liabilities the company is not actually doing as well as the assets imply.”

Laine: “I think that could work the same for revenues and expenses though. A company may show a lot of revenues but be weighed down by expenses.”

Kate: “However, a good part of option one is when it comes to a company acquiring another by buying assets directly rather than stock, companies are able to enter different markets and increase revenues.”

Laine: “That’s true, I think you could see a company's liquid value better using viewpoint one.”

Olivia: “I think this is better suited for companies that are already established, since, yes, entering different markets is a positive, but new businesses first need to get started before they start taking on other ventures.”

Mary Grace: “An issue that could occur due to viewpoint one is stockpiling. Companies might take this viewpoint and run with it, growing their production to greatly exceed the demand for their product.”

Laine: “Let’s move on to viewpoint two. Any ideas?”

Mary Grace: “Viewpoint one had some good ideas, but some companies do not revolve around asset growth, especially when you take into account small businesses.”

Kate: “I completely agree with Mary Grace. Growth is important, but not as important as profitability especially considering that the purpose of financial reporting is for external users. Profitability is more telling, in my opinion, of how a company is performing.”

Laine: “Yeah, I think this is especially true with small service companies where you may not need a lot of assets to bring in revenue.”

Olivia: “Like Kate said, this choice shows profitability, and profits are needed to purchase those assets discussed in viewpoint one. You cannot just acquire assets without capital. I guess you could say they could borrow in order to purchase the assets, but lenders would not want to assume the risk of lending to companies for which they cannot see how much profit they are making.”

Olivia: “Viewpoint two is very cyclical. While both are looking at asset change, two is not just acquiring and, like Mary Grace said, “stockpiling” them. The assets are being used in order to create more assets, leading to earnings being brought in and retained. This process would make much more sense for manufacturing companies since they buy materials, which are used as assets, to create more product and profit off of the difference in cost and selling price. These earnings then go back into the bank to be used for future production, with an addition to the amount each time more product is made.”

Kate: “I was thinking the same thing, Olivia. Viewpoint two immediately made me think of manufacturing companies. Since most examples we look at in class are manufacturing companies I think that’s why it makes more sense to me that focusing on revenue and expenses is more important and useful to financial reporting. Like I said earlier, financial reporting is supposed to be for external users.”

Laine “Because of that, I think this viewpoint is easier to see how well the company is currently operating and bringing in revenues. You’re not just looking at assets that could have been acquired years or even decades ago; you can see what they brought in within the last operating cycle.”

Mary Grace: “This viewpoint is more beneficial for external users, as it focuses on revenues and expenses which are found in the income statement and because external users are very concerned about profitability. This is the biggest reason that leads me to agree with viewpoint two more than viewpoint one.”

Laine: “Going off of what Mary Grace just said, this could also be a little dangerous. You could have one period that shows a high profit, but you can’t tell as much if the liabilities aren’t displayed.”

Mary Grace: “So we all agree on viewpoint two? Should we move on?”

<u>Question 2:</u> Read and consider the following two viewpoints. Discuss which viewpoint should be the FASB's focus when promulgating new standards. Take excellent notes of your group's discussion and write a fully developed brief highlighting the pros and cons of each viewpoint culminating with a final decision based on the consensus of your group. Explain why that viewpoint won the debate.

Mary Grace: "In viewpoint one, companies realize value on assets once they are exchanged or sold. This is problematic because the assets would have no value on the financial statements until the assets are sold."

Kate: "Well, they would have value as assets on the balance sheet, just not on the income statement until after being sold (revenues). I think the key is 'firm-specific' value but I'm a little confused about what that means exactly."

Laine: "The way I understand it is value added to a company from using their specific assets. It's something that another company probably wouldn't value as highly."

Olivia: "Right, this viewpoint leaves out work in progress, so we could not see how each input is affecting the good as a whole. This may simplify the accounting process when looking at how much a product is costing the company compared to the benefits it brings since rather than having each individual input into the product, it is condensed into just the product itself."

Mary Grace: “Going off of Olivia’s thought, this viewpoint is dependent on the market price of the good or service a firm is providing rather than the value of the materials it required to make the product.”

Laine: “Yeah, that’s true, it would make the value of all of the assets a lot less subjective.”

Olivia: “If we do not standardize value, who is to say what something is worth? There is no firm-specific value with this option since the company is only receiving that monetary gain from the exchange or sale of the asset.”

Kate: “I feel like viewpoint two would better show expenses allocated/traced evenly across each period as well as better matched with revenues. It takes into account future cash flows and assigns its value based on that, rather than just the market price at the time of sale.”

Mary Grace: “That generated firm-specific value is more valuable to an internal user because firm-specific value is subjective. However, it does create more value in the firm other than cash.”

Olivia: “Exactly, it is not very useful in external reporting because companies are going to be uninterested in what other companies have for firm-specific value since that value cannot be monetized.”

Kate: “I think that viewpoint two is more relevant to a company that uses an asset over time. Especially something nonrenewable like a paper company that chops down trees. The trees are consumed over time and in turn add value to the company when the paper made from it is sold.”

Mary Grace: “Kate, I like that example because it shows how the in-use asset is adding value to the firm. In the example, the value of the trees is depleting while the value of the paper increases, creating firm-specific value.”

Olivia: “From what I understand, you would be decreasing one account as an asset is being used while at the same time increasing another account for that same example. For example, like how equipment is depreciated, and an amount is credited from the equipment’s asset account but debited into depreciation expense for that equipment. Is this how you guys see this?”

Kate: “Yes, as the equipment is being used the company would depreciate it by debiting depreciation expense and crediting accumulated depreciation. Equipment is reduced not decreasing the equipment directly but through the accumulated depreciation account. Accumulated depreciation would show up on the balance sheet and the value of the asset as a net amount.”

Laine: “I agree, but what would the account credited be in this case? Some sort of contra-asset, right?

Olivia: “I have not found a contra-asset that would work for this, so I think there would have to be a new one made. We seem to have found more advantages for viewpoint two, does everyone agree?”

Mary Grace: “I agree, viewpoint two definitely makes more sense to me.”

Kate: “Definitely.”

<u>Question 3:</u> Based on your answer in Question 2, how will current accounting have to change to accommodate this value definition? Provide examples of specific transactions and how their journal entries (either accounts or amounts) would change under this new definition.

When buying machinery with cash, not only will we receive that machinery as an asset, but we will also be acquiring the asset of firm-specific value.

<u>BUY:</u>

Fixed Asset	20,000	
Firm-Specific Value	5,000	
Cash		25,000

DEPRECIATION:

Depreciation Expense	6,000	
Firm-Specific Value (asset)		1,000
Accumulated Depreciation (contra asset)		5,000

SELL:

Cash	25,000	
Accumulated Depreciation	5,000	
Fixed Asset		20,000
Firm-Specific Value		4,000
Gain On Sale		6,000

As a health food store owner, you buy a plot of land next to a gym on which to build another store. Because you will have many customers who are members of the gym next door, this plot of land has more firm-specific value than a plot of land across town.

BUY:

Land	100,000	
Firm-Specific Value	10,000	
Cash		110,000

SELL:

Cash	110,000	
Land		100,000
Firm-Specific Value		10,000

Your company has a factory designed to unique specifications that allow you to carry out your operations more efficiently. Because of this specificity, other companies would not be able to operate as well, so they value the factory less since they do not operate exactly as you do.

BUY:

Factory	100,000	
Firm-Specific Value	20,000	
Notes Payable		120,000

SELL:

Cash	120,000	
Firm-Specific Value		20,000
Factory		100,000

III - Analysis of *Taxodus – Playing the Global Tax Avoidance Game*

Introduction:

The purpose of this case was to evaluate the effects of the corporate income tax on the economy. As a preface, we were to watch the film "*Taxodus*." This documentary shows the process that rich multinational corporations go through to offshore their profits in order to pay less taxes on them as well as the effects this has on both the countries who are missing the taxes as well as the countries being taken advantage. Using this information, as well as data about the U.S. economy following the recent corporate tax cuts that stemmed from the Tax Cuts and Jobs Act (TCJA), we were to form our own opinions about what the corporate income tax should be. Additionally, we were to discuss if our desire to work in the field of tax had increased or decreased after this case.

I think this was a good case for me because it got me to look deeper into the tax codes of our country, and all their troubles. Researching the effects of the corporate tax rate certainly opened my eyes to a number of things that I had never thought of before and will certainly influence my thought process about tax laws going forward. I also found it interesting to see the myriad of ideas put forth about how to amend and even rewrite our tax codes, and I know that I will have to do a lot of subsequent research in order to solidify my opinion on the matter.

Also, I think the question about whether our interest in the field of tax had changed because of the case was a real revelation. I think it was valuable experience to get to see the worst part of the field highlighted so that we could have a better understanding of the true nature of how these laws affect the real world. Overall, I think this was one of the more informative cases for me, and it was especially important to examine these aspects of the economy right before an election.

Question 1: What do you think the optimal corporate tax rate should be and why? Explain your answer including information gleaned from the two links and the documentary.

There are few things in politics that are as divisive as taxes, and the corporate tax rate is no different. People from all sides of the political spectrum endlessly argue the effects of their ideal corporate tax rates and espouse grand idea about closing loopholes, mostly to no avail. My thought is that there is no ideal tax rate because of the lengthy and convoluted nature of the tax codes. This combined with the lack of global cooperation in our increasingly globalized world means that wealthy corporations can funnel money through complex channels and pay little to no taxes which leads to governments running on deficits and capital sitting idle while the rich grow increasingly rich. The only way to prevent this and eventually settle on a tax rate that benefits everyone is to make giant leaps to modernize and globalize the way we perceive and enact corporate taxes. I propose two wildly different rates ideas for the ideal corporate tax. The first is a 26 percent rate that is contingent on several factors, and the second is abolishing the corporate tax altogether.

My first idea seems pretty mild on the surface level. I chose this rate because I think it walks the fine line between benefiting businesses and funding current and future government expenditures. A 26 percent corporate tax is only slightly higher that the worldwide average of around 24 percent and is on par with the same rate weighted by GDP which is just above 26 percent (Asken 2019). Being this close to the average tax level still gives us an advantage. Corporations want to do business here due to our vast economy and skilled and educated workforce, so being anywhere near the average tax level will draw in business and keep our current businesses here. Additionally, keeping our tax rate lower than the proposed 28 percent saves businesses money that they can in turn spend on increasing their capital stock. This increases productivity and subsequently worker's wages (Hodge 2018). These factors will allow us to enjoy some of the benefits caused, at least in part, by the current tax cuts such as lower unemployment and GDP growth (Department of the Treasury) On the other hand, raising our corporate taxes back to a higher level will help reduce our ever-growing deficit spending which reached almost one trillion dollars in 2019 (Horsley 2019).

The problems with this 26 percent tax rate arise when large, influential companies start claiming that this rate is too high and begin using backchannels and shell corporations to store money in tax haven where they pay little to no taxes on their earnings as is shown in the documentary "*Taxodus*". From here, we have two options. First, we can give in and lower taxes, and some money will flow back into the country. Eventually, this money flow will slow, as it already has in the U. S's case, and more cuts will be demanded (Dmitrieva and Davidson 2019). This "race to the bottom" as it is described in the movie is a real phenomenon that only leads government deficits and more offshoring of money. The fact is that we will never be able to compete with the low tax rates offered by some countries and that corporations and their army of lawyer and accountants will always find ways, legal or not, to avoid paying their share of taxes under the current system. This hurts the country by reducing its much-needed revenues as well as smaller business that do not have the means to offshore their profits. That is why there is only one real option going forward: to completely rethink and rewrite the way we manage taxes in our country.

One of the main aspects of the tax system that needs to be reformed is the use of deferments of overseas profits. This is one of the most damaging points in the tax system because it encourages companies to offshore profits to avoid paying taxes. One solution is to have tax holidays where companies can bring in this money at drastically reduced rates, but this just leads to payments to stockholders and stock buy backs, not reinvestment into the economy (Dharmapala, Foley, and Forbes 2010). A better option would be to tax all of this this income at the time it is made. This would bring additional revenue, but it would ultimately lead to more shady business practices and avoidances. The best plan, and the ultimate goal of my "ideal corporate tax rate" would be a more globalized agreement on how multinational corporations should function and be taxed.

Though this part of the plan would be difficult to see through, I think the end results would be worth whatever effort is put into it. Our tax codes are outdated, and no amount of patching will make them efficient in modern times. Today's businesses are increasingly global and increased infrastructure throughout the world and the internet will only expand this. By coming together with the other nations and rewriting and simplifying our tax codes based on the best taxation policies going forward, we could modernize the way we tax businesses in an increasingly globalized world. This would broaden the tax base reduce the need for higher taxes. This would not only help the countries whose taxes are being avoided but also the tax haven countries. This could prevent large companies from taking advantage of those countries lax policies and then leaving, contributing little to the country. I cannot say exactly what would be included in the new, modernized tax laws, but I would think it would place restrictions of flow through entities and other methods used to offshore profits as well as agree on how to tax multinational corporations that is equitable for the largest amount of people. While this all might seem hopeful, I think there is a growing movement to devise a better system based on how modern businesses operate.

My second idea for an ideal corporate tax rate—reducing the rate to zero -- is much more controversial but has a lot of support among economists. *The Hill* summarizes this plan nicely; replace the loophole ridden corporate tax with a revenue-neutral consumption tax (Jordan and Miller 2018). The basis for this plan goes back to introductory economics by pointing out the fact that taxes distort supply and demand drive up prices for everyone. By eliminating this distortion, products are at their natural equilibrium price and therefor more beneficial to everyone. To make up for the lost revenues, the government simply institutes a tax on consumption such as a value added tax (VAT) that is becoming increasingly popular. Because they are only being taxed on what they consume instead of their profits, businesses have more incentive to reinvest profits and maximize their use of resources according to the *Planet Money* podcast sponsored by NPR (Planet Money). Additionally, this taxation method could be tweaked to benefit companies deserving of tax breaks or subsidies in a much more efficient manner. The fundamental issues with this approach are the potential complexities of it, especially during the transition period (Worstall 2017). Though I admittedly do not know the solution to the problems presented by this method, it does not mean they cannot be solved. From what I understand, I truly believe this could be a reasonable answer to the tax woes our country faces, and it doesn't have to stop at just the corporate tax rate, the economist in the Planet Money podcast gives great supporting evidence as to how this method could be used in place of many different forms of taxation to make our system much more efficient and progressive.

Question 2: Did this case increase or decrease your interest in pursuing a career in the tax service line? Explain your position.

Admittedly, as I was watching *Taxodus*, I became discouraged about a job in the tax service line. As mentioned by economist James S. Henry in the documentary, I did not want to become one of the 'baddies' that helped contribute to this corrupt system of tax evasion and exploitation. I personally believe that paying your fair share of taxes is the right thing to do as long as it is being spend reasonably, so the idea of helping giant multinational corporations avoid enormous amounts of taxes was troubling for me. I understood that going into that line of work would involve minimizing taxes, but the level to which it is happening every day and the amount of pure exploitation and shady business practices that occur really surprised me. Later, as I began doing further research for my paper and seeing all the people who work tirelessly to influence the tax laws for the good of the people restored my faith in the field. Doing something of this nature is really interesting to me. I think one day being able to influence tax policy in a way that makes it simpler and more equitable for people would be rewarding beyond measure. So, overall, I think this increased my interest in the field.

IV - Interview of a Professional

Introduction:

For this case, we were supposed to reach out to someone who has an established career in the business community and interview them about their life and career. Then, we were supposed to turn this into a mini biography about this person. From this process we were supposed to take this information and use it as a learning experience for ourselves about the important decisions we are soon going to have to make about internships and future jobs.

As my interview subject I chose Shawn Landrum. He is currently the controller at a shipbuilding company near my hometown and is someone I consider to be successful, as well as my partner's father. For the interview process I used the provided question list as well as additional related questions to help draw out his answers when I did not think the original answer was long or specific enough. This interview also led to a much longer conversation about the business world and his past that is beyond the scope of this interview but was a wonderful learning experience.

This case came at a perfect time for me. At a time when I am preparing to apply to internships, it did me a lot of good to listen to the wisdom of someone who has gone down a similar but slightly different path than the one I am about to take and became rather successful. The conversation helped me better align my priorities and showed me the impact of these imminent decisions. It also motivated me to set a new focus on learning the technological aspect of the accounting field as well as dedicate to memory some of the often-overlooked processes. Finally, I was inspired by all the wisdom bestowed on me and was moved to take on more risk in the future while still remembering to take care of others along the way. Overall, I think I am very lucky to have such a great resource to draw knowledge and insight from in my future endeavors.

Early Life:

In his early life, Shawn attended a very small private school near Pascagoula, Mississippi where he grew really close to all of his classmates. Any sport that they could gather enough players to participate in was very important in the small school, but he was never really interested in them. A lifelong outdoorsman, he preferred to spend his free time hiking, camping, and generally enjoying the natural world. In fact, his first glimpse of the business world was raising and selling rabbits as a kid.

According to Shawn, his time in college is hard to sum up because he spent around ten years getting his degree, and a lot changed during that time. He attended the University of South Alabama and began college interested in many different fields and subjects, but with no feel for what he ultimately wanted to do which made it difficult to settle on a single major. He spent several years switching between various business and STEM majors, taking courses that he was interested in (including volleyball multiple times). During this time, he also worked several jobs in carpentry and at an oil refinery to help pay for school. He even briefly fulfilled the accounting role for a man who owned a business that installed flooring and granite as well as a small shipping company which gave him an appreciation for the field.

After attending college for many years with no clear direction, things changed drastically when he fell in love, got married and had a child. He then decided that, based on the experience he had and the classes he already completed, accounting was the best path forward, even though that had not been his original plan. With a clear path, he focused on his schoolwork and finished his degree shortly after.

<u>Career:</u>

Before graduation, Shawn obtained a staff accountant job at Keithly Aviation. During his time at the small company, he worked his way all the way up to controller. While working here, he improved many accounting skills that helped him throughout his career and gained proficiencies in management before deciding to move on to better things. His next job was as an accountant for the Boy's and Girl's Club in Mobile, Alabama. Though he did not spend much time here, he got to see the profound impact you can make as an accountant.

After leaving the Boys and Girls Club, Shawn took a job at what is currently Huntington Ingalls Shipbuilding in Pascagoula, Mississippi. During his many years at the company, he worked his way up through many different jobs. He started in the finance department before eventually moving on to strategic planning and then cost accounting. During this time, he continued to hone his accounting acumen and gained knowledge in IT and cybersecurity. With this knowledge, he moved up to the accounting manager for the IT department where he spent several years. During this time, he improved his management skills, learned more about emerging technologies, and became comfortable with managing larger budgets.

Recently, Shawn has taken a job as the controller at VT Halter Marine, another shipbuilding company in the area with around 1,000 employees. Though he is still adjusting to his new job, he really enjoys the challenge and the new experience. Though it is more difficult than his previous jobs, he is looking forward to continuing to improve his skills and learn more about the field and the company.

Personal Life:

Outside of work, Shawn says that he has a fulfilling life and is still a fan of everything outdoors. He tries to spend all of his time outside of work hiking, kayaking, or biking everywhere within driving distance of his home, especially with his family. Whenever possible he also loves to travel, and he has been many of the U.S. National Parks, a substantial portion of states, and several foreign countries. His favorite vacation he has ever taken was his trip to Guatemala with his wife early last year where they stayed on Lake Atitlan and hiked on an active volcano. He said he is also excited about all of the trips he has planned for the future and all of the bucket list boxes he is going to be able to check after retirement.

When asked what he was most proud of he quickly responded with his family. He said he has thoroughly enjoyed not only the things they had gotten to do together but also all of the time they had spent together and all of the events he was present for because of the flexibility of his job. On the other hand, he said if he could change anything about his life, he would have taken more chances in his decisions and been more open to moving throughout his career. Additionally, he said that he wished he had prepared more for retirement early on in his life, which is a sentiment he said he hears all too often.

Knowing what he knows now, he gave me one piece of advice and two quotes. The advice is to be flexible in all aspects of your life. This, he said, means taking on more risk, but it also means possibly opening up better doors that you may not have previously seen. The first quote is attributed to the famous motivational speaker Zig Ziglar: “You can get everything in life you want if you will just help enough other people get what they want.” This quote struck me as odd, but it did remind me of the importance of generosity and helpfulness in the often overly competitive business world. Second is a quote of his own that I have known him to live by: “if your boss asks you to do something, say yes; you can figure out how along the way.” Though it sounds silly and is probably a bit of a hyperbole, it reminds you to take risks and to also continue to learn and perfect your skills, especially if it is at the request of your boss.

Challenges of the Future:

After the more personal questions, I asked him what he thought the biggest challenge for his generation is going to be. He replied that hopefully soon his biggest challenge will be figuring what to do with all his free time during retirement. In all seriousness, he said he thought their biggest challenge will be managing the changing work culture. He said since people his age are the ones in management positions at this point, they are seeing a lot of pressure to adapt to things younger people are looking for in a job such as more flexible schedules, shortened workweeks, and even working from home. He admitted that he would love to see all of these changes. He said that he had been lucky enough in the past to have a flexible schedule and even work from home when the need arose, so he saw the value in all of the requests and said they are both reasonable and necessary things for people to ask for. He also indicated that just because he agrees with the changes that does not mean implementing this is not difficult. It brings up logistics and accountability issues as well as security problems when employees are working with more sensitive information. The past year has certainly shown that meeting these demands is a real possibility he insisted. The other change that he has seen is a reduced loyalty to the companies you work for. People now are far less worried about switching jobs than they used to be, and that pushes them to work harder to implement these changes and create reward structures that attract new employees and help keep the older ones.

Finally, I asked what he thought is the biggest challenge facing my generation. He thought that one of the biggest challenges we are going to have to deal with is embracing all of the fast-paced technology changes while not losing sight of the basics of what it means to be an accountant. Keeping up with changes is always going to be tough he stated, but now it seems like they come along faster than when he first started his career. He thought, for the most part, the technology changes he has seen have been great; They cut down on a lot of the menial work that consumed so much time previously and allow people to focus on deeper issues. The problem with this is that often doing those tasks over and over gave the workers a deeper understanding of what is actually happening which allowed for better decisions to be made. Increasingly, he said he felt the younger people are becoming more disconnected from the numbers they are working with, and there is potential for this to get worse as more advancements come. He said that as a manager he could bring almost anyone in and have them put numbers into a computer, but that is not what they are looking for. What he wants is people who have a firm understanding of what those numbers mean and all of the processes and other intricacies that go into creating them because those people are going to help him make better decisions and add real value to the company.

Conclusion:

In conclusion, while it may have been a bit awkward at first asking all of these questions, it gave me a better insight into a person I have known for several years now, and it shed a light on how he has made it this far in a successful career. I got a unique perspective about the internships and jobs that I am currently looking into from someone who has had firsthand experience in these same decisions. Additionally, I received an inside look at the perceived challenges in the business world for my generation from someone who is at a similar position to the people who will hopefully be hiring me in the near future. This gave me a lot to think about and is invaluable information as I continue my education. Finally, I drew inspiration in hearing this story about this climb to success, and the wisdom shared will undoubtedly stick with me for a long time coming.

V - CASE COMPETITION - OVERVIEW

Completed by a group consisting of deYampert Garner, Laine Keel, James Mclemore, Jamison Russ, Cristina Trefry

Introduction:

This week our group was tasked with picking out a company to study and research. The company chosen would then be the subject of a deep investigation to the ends of a group presentation in the coming weeks. The research and subsequent presentation are taking the place of the case competition traditionally completed in this course. Our group chose Pfizer to present for our case study and began researching using the suggested websites.

Discussion:

Pfizer is one of the world's leading pharmaceutical companies. Based in Manhattan, they annually report sales of over $50 billion dollars and spend close to 20 percent of their sales on new research and development costs. Their products span across healthcare fields from generic, over-the-counter medications to immunotherapy drugs and cancer treatments.

Pfizer has grown largely through acquisitions. They have grown organically, of course, through their own generation of medical products (Wikipedia). Worldwide Research Development Medical (WRDM) is their research and development branch, and they have over 90 new products and improvements currently in the works. Mergers do, however, account for a substantial portion of their increasing size, especially in the 2000's. The largest of these combinations occurred in 2015 when Pfizer acquired Hospira for over $15 billion; the synthesis of the two companies made Pfizer the largest producer of injectable pharmaceuticals in the world. Although not all of their proposed mergers have been successful, as displayed in their Allergan acquisition attempt, they have had recent success through one of their subsidiaries, Upjohn. Upjohn has recently begun managing Pfizer's Meridian subsidiary which specializes in auto-injectors, the most well-known of which would be EpiPen. Shortly after the change in management, Upjohn combined with Mylan to form a new company, Viatris, which will continue to operate both Mylan and Upjohn business under new ownership. While Viatris is their most recent development, the acquisition of Array for over $11 billion in June of 2019 marks another milestone in their growth.

Pfizer is using many of these mergers to help to expand to new markets. They are putting forth a concerted effort to develop market share in emerging markets such as Asia (excluding Japan and South Korea), Latin America, Eastern Europe, Africa, the Middle East, Central Europe, and Turkey. This diversity in markets does expose Pfizer to risk from the fluctuations in foreign exchange rates, but they hold a number of securities contracts to hedge this risk. The SEC has taken notice of Pfizer's growth in many of these markets and has fined them for bribing foreign officials to pass their drugs through inspections.

Alongside the SECs watchful eye, Pfizer is under several minor investigations, although none of them seem to be crippling in nature. Investigations include subpoenas and inquiries from the United States government surrounding operations in India, China, and Russia. Pfizer is also facing several class action or multi-district lawsuits surrounding their products; pricing of their EpiPen and several of their other products constitute most of these civil suits. Some malignant effects of Viagra and Docetaxel, a cancer drug, are also on trial in a number of states. They have entered settlements on all environmental related issues, which have been ongoing for decades. In March 2020, another long-lasting suit was settled surrounding hormone therapy drugs sold under a subsidiary, Wyeth. Conversely, Pfizer is also the plaintiff in a number of patent-related suits against other pharmaceutical companies.

Beginning in 2018, Pfizer had a five-year plan to invest approximately $5.0 billion dollars back into the United States. As part of this plan, the company announced in mid-2018 that they would be investing $465 million into a state-of-the-art injectable pharmaceutical production facility in Portage, Michigan (SEC.gov). This boost to the facility has been instrumental in the production effort for the Covid-19 vaccination. Additionally, the company stated plans to invest close to half a billion dollars to construct a new gene therapy production facility to boost their research and development capabilities. To give back to their employees, Pfizer voluntarily contributed $500 million to their pension plan and gave out one-time bonuses to their employees totaling $119 million in early 2018.

Pfizer's 2020 plan was abandoned due to the worldwide pandemic (SEC.gov). The coronavirus has caused Pfizer to shift gears to developing a vaccine. The vaccine was declared to be 90 percent effective nearly a week after Election Day. This caused noticeable spike in Pfizer's stock price. Since millions of vaccines would be needed by the US Government, as well as others, focus has shifted to producing those vaccines in a timely manner since the main competition, Moderna, produces a vaccine with similar efficacy rates - within one percent - that is easier to store and lasts longer (Branswell et al). Availability is the key to making this pandemic as profitable as possible for Pfizer since they are fighting with a more agile competitor. Pfizer's chairman and CEO, Dr. Albert Bourla, was looking to continue regular research and development processes throughout 2020 according to his letter included in Pfizer's proxy statement (SEC.gov). To be one of the companies developing a vaccine for the COVID-19 pandemic was not expected, but they have adapted to the situation and have been able to turn in a profitable and productive year.

Conclusion:

In this case, our group gained an understanding of how Pfizer operates and the way it has developed in the last five years. A particular focus was on the mergers of Pfizer and the coronavirus vaccine they developed. This baseline of knowledge will allow our group to provide a more insightful analysis of Pfizer as we continue in this case study.

VI - CASE COMPETITION - AUDIT

Completed by a group consisting of deYampert Garner, Laine Keel, James Mclemore, Jamison Russ, Cristina Trefry

Introduction:

For the second week in preparation of the case presentation, our group was given a brief introduction to the process and goals of auditing since none of our members have taken the audit-specific class at this time. With this new information, we searched through the income statement and balance sheet of Pfizer looking for potential signs of a material misstatement of six accounts. In addition to the risk of misstatement, we were tasked with assessing the risk associated with the misstatement and suggesting internal controls to prevent inaccurate reporting. These solutions were applied using data analytics to evaluate balances and transactions.

Revenues:

Revenue marks the beginning of the income statement. Misstating revenue then, has the potential to distort earnings reports and, depending on the magnitude and direction of the error, a misstatement could drastically under or over state Pfizer's performance for the year. Revenue is an audit risk because of the magnitude of transactions that are aggregated in the account, and revenue's significant size makes it especially important to accurately report the account. Pfizer is one of the forerunners in pharmaceuticals in terms of digital supply chain management and cloud-based information controls. The massive scale of their selling process, however, means that simply looking at a log of transactions would not rectify the risk of misstatement. A randomized sample of transactions from each geographic region should be taken, and the money in the account should be traced from the purchaser of the inventory to the deposit in Pfizer's balance.

A significant reason for reductions in the revenue account is contra-revenue accounts that are not on the face of the income statement. Gross sales would have been 40 percent higher than reported revenue if these contra-revenue charges that were included in the initial report (SEC.gov). One-quarter of this 40 percent reduction of gross sales comes largely from chargebacks (allowance accounts) from U.S. wholesalers who make up over 35 percent of Pfizer's global, annual revenue as reported in the income statement (SEC.gov). While there may not be a data analytics solution to these numbers, a closer look at the contracts would be insightful.

Long-term Debt:

Another risky account our group chose was long-term debt, specifically the completeness of this account. Long-term debt makes up approximately 35 percent of Pfizer's total liabilities (SEC.gov). Understatements of long-term debt could have major effects on a company's balance sheet. There are great risks valuing long-term debt, and it is important to conduct internal controls when doing so. Two internal controls that could be especially useful in creating an accurate representation on long-term debt are segregation of duties and routine market tests. Segregation of duties allows for more than one person to evaluate portions of long-term debt by separating the authorization of borrowing from the record keeping of the debt. Another internal control that could be useful for long-term debt would be conducting routine market tests. Updating present values on long-term debt is important to make sure the values are accurate.

Goodwill

Goodwill represents 35 percent of Pfizer's total assets (SEC.gov) Since this amount makes up over one-third of the company's assets, we believe goodwill deserves further inspection. Pfizer continually seeks to acquire other companies to capture new markets, ideas, and products, and these actions lead to significant goodwill balances. Acquirers often overpay for the target and the acquisition premium increases goodwill balances. Goodwill is not routinely amortized as a charge against net income, but it is tax deductible; meaning that cash tax savings are realized without a corresponding reduction in book income. Behaviors like this keep taxes lower while expanding revenues which keeps stock prices soaring. As well as stockpiling goodwill, Pfizer also writes off very little goodwill due to impairment. In fact, during 2019, no goodwill was written off as impaired during their goodwill impairment review and none was determined to be at risk of being impaired in the near future (SEC.gov).

Pfizer does organize a regular goodwill impairment review which greatly lessens the risk of this practice. An official audit would surely check into the processes and notes of these meetings to ensure that honest appraisals were given of all material acquisitions. Assessing these transactions would require an analysis of the companies that were acquired and the book values at which they were acquired. Streamlining this process would require impairment tests to be automated. Keeping separate records of the acquired companies would allow for their book values to be evaluated regularly, and the resulting impairments (or nonexistent impairments) would be entirely automated. This would be a great use for data analytics because of the substantial number of mergers and acquisitions that Pfizer engages in.

Accumulated Other Comprehensive Loss:

Accumulated other comprehensive loss represents over $11 billion in losses on the balance sheet, which is always a cause for concern (SEC.gov). One reason that this is concerning is because over half of this balance comes from a loss on foreign currency adjustments which is a loss that is hard to control due to the volatile nature of some foreign currencies. Another cause for concern is that these losses on foreign currency adjustments are carried over year-to-year, and the statement gives no indication if the values are adjusted for inflation or even the current value of the reciprocal currency. Finally, the report shows that there has recently been a change in the accounting practices related to this account. This calls into question whether carried over amounts from the previous years are accurate and whether more research should be conducted to verify that these numbers are in fact correct.

Another generous portion of the loss from this account is attributable to actuarial losses from the company's benefit plan (SEC.gov). This amount should also be verified because it isn't clear if this financial risk is adjusted either. There are certainly ways that technology could help with certifying these numbers. One way is making sure the most up-to-date valuation of currency is used and keeping track of currency values to help reduce the risk of these losses in the future. Another is using processes to ensure that the people responsible for assessing the risk of the benefit plan have all of the relevant and current data to make their decisions. The good news is that the company is reclassifying some of both of these values, meaning that it at least acknowledges the importance of verifying and adjusting these values.

Research and Development:

Pfizer's research and development (R&D) expenses mainly come from collaborations or licenses with other companies. Pfizer collaborates with both partners and third parties, but only lists partners in the notes of the income statement. R&D is also funded by licensing agreements, with Pfizer currently in three major license deals (SEC.gov). R&D within Pfizer runs several risks, one of which is dealing with external factors. Most of Pfizer's R&D comes from collaborations and licenses with other companies, and these partnerships come in the form of multi-million-dollar deals. A potential deal not going as planned runs the risk of sizable portions of funding that are in R&D being forcefully retired or removed. The other main issue with R&D is regulatory. Pfizer can allocate a large fund of money to a product and have the product rejected based on regulations. This recently happened to Pfizer with their autoimmune disease drug Xeljanz which failed regulatory FDA drug tests earlier this week.

As stated earlier, Pfizer only releases a list of funding they get from large partners, which makes up a small portion of their R&D expense. Creating a list that includes the funding from third party transactions will allow for Pfizer to run less of a risk. The use of data analytics would allow auditors to possibly see the greater breakdown of the R&D account. Data analytics could allow for the possibility to see where the funding for R&D is coming from and how R&D is expensed over the company. Data analytics would add an extra layer of protection over R&D and allow transparency.

Conclusion:

This case was a learning experience for our entire group. We were able to learn a basic understanding of what auditors do and apply that to our company. While the process took time and patience from our group to gain these basic understandings of audit, our group managed to successfully find what we believe to be the six riskiest accounts under Pfizer. This case helped our group gain both an overall understanding of audit and of Pfizer’s financial transactions that will hopefully be useful as we transition to tax.

VII - CASE COMPETITION - TAX

Completed by a group consisting of deYampert Garner, Laine Keel, James Mclemore, Jamison Russ, Cristina Trefry

Introduction:

For the third week of case competition preparation, our group's assignment was to formulate strategies to elicit tax savings for Pfizer. With minimal experience, the group was given a set of recently implemented tax regimes as a starting point for our analysis. The plans for savings can come from restructuring, expansion, or divestiture, but should be accompanied by supporting figures that specify the magnitude of the savings and an outline of the process by which Pfizer will change its current strategy.

Because of the confidential nature of taxes in general, a degree of uncertainty exists regarding what Pfizer's current strategies are, and so our suggestions may reflect strategies already being considered or implemented by Pfizer. Additionally, errors in the assumptions we make about their current position may affect our predictions. As a pharmaceutical company, Pfizer has two potential areas within which to improve their already impressive 7.8 percent tax rate from 2019: intellectual property and research and development (SEC.gov).

GILTI Tax:

The GILTI tax updated in the Tax Cuts and Jobs Act may pose a hurdle for Pfizer, who has substantial positions in pharmaceutical patents which produce royalty income from allied sales. Although not disclosed in their financial statements, it is customary practice for large companies with significant intellectual property to house their revenues generated from these assets in foreign subsidiaries. Since Pfizer has considered moving its entire operation to be headquartered in Ireland through the purchase of Allegan, and Ireland has friendly, globally renowned tax practices, we will assume that they house a significant amount of their intellectual property there. The amount of GILTI tax is dependent on the amount of depreciable, tangible assets the foreign subsidiary holds. Any income over a 10 percent return on these tangible assets is considered to be taxable under GILTI. So, increasing tangible assets decreases the amount of GILTI tax by 10 cents on the dollars.

The pharmaceutical industry is facing changes in the near future because of their current dependence on patents to be able to control the distribution of new medicines. In having to implement more service-oriented infrastructure, this reduction in GILTI tax would provide an incentive to move forward with investment in tangible infrastructure in the health service industry. Pfizer has consistently received $500 million in royalty revenues (SEC.gov). Assuming that $400 million is taxable under GILTI at a rate of 10.5 percent, investment of the full amount in new infrastructure would provide a tax saving of $42 million. Of course, Pfizer would not spend $400 million to decrease their taxes by $42 million, so the project in question would need to be profitable in itself to validate the spending.

Additional U.S. Tax Credits:

Our second strategy would be to reduce research and development (R&D) conducted in Sandwich, U.K. by half and then relocate that portion of the R&D to facilities inside of the US. This move would allow Pfizer to take advantage of the 10 percent tax credit proposed by President Joe Biden that is given to corporations that bring foreign jobs back to the United States (Amadeo 2021). Pfizer spends $374,544,000 on R&D at their U.K. facility, so half of this amount, $187,272,000, would be rehomed to the seven U.S. research facilities in order to create jobs and qualify for the tax credit (SEC.gov).

Based on the tax rates of the two countries and the new tax credit, Pfizer could save nearly $200,000 on this move alone and create substantial amounts of goodwill with the American public and the current administration. On the other hand, the value added by this facility -- owed to its connection with the U.K. government and important Asian partners -- means that it is unwise to move all of this production back to the U.S. Additionally, this strategy relies heavily on the tax credit being implemented, so Pfizer should monitor the political climate to make sure this is being enacted.

Conclusion:

Pursuing the expansion in the amount of depreciable, tangible assets is a method that will simultaneously increase the amount of future revenues while decreasing the GILTI taxes that accompany such increases. This is a strategy that will allow for Pfizer to continue to take advantage of Ireland’s favorable tax policies even with the stricter GILTI tax. The second tax strategy of moving half of the Sandwich, U.K. research and development operations to the United States to take advantage of President Biden's recent 10 percent tax credit for creating new U.S. jobs will allow Pfizer to decrease taxes while maintaining the same level of research and development (Amadeo 2021).

Moving half of the R&D operations will enable Pfizer to take advantage of the tax credit while also maintaining their multinational relationships. While tax savings of the move are not substantial, they would provide considerable amounts of goodwill that will be worth significantly more than the tax savings. Overall, Pfizer already has an impeccable record for reducing taxes, but they would be able to further improve upon their taxes by taking advantage of new tax laws that have been put in place by the Biden administration.

VIII - CASE COMPETITION - ADVISORY

Completed by a group consisting of deYampert Garner, Laine Keel, James Mclemore, Jamison Russ, Cristina Trefry

Introduction:

The third week of the case competition asked the group to analyze Pfizer's current weaknesses and strengths. From there, we were to brainstorm new, innovative ideas to address areas of weakness and/or threats that would positively impact the financial statements and their respective ratios for the years to come. Pfizer is an extremely agile company that is constantly growing in new areas and broadening their horizons, which made this difficult. Because of this, new ideas were sparse, but when we began to discuss the different threats more in-depth, we were able to find areas to which they had not expanded. They have not begun to explore the holistic wellness and healing that is becoming increasingly popular. We believe that Pfizer could acquire a small company that has done significant research in this area that Pfizer could easily expand upon. Secondly, we suggested that Pfizer take advantage of people's desires for convenience and implement a direct-to-customer shipping division in larger cities across the United States.

As a group, we were able to learn to think analytically about a company and their strengths and weaknesses in a prospective manner. This was a unique challenge that allowed our group to collaborate in order to find effective solutions that can be profitable for a multi-national company with billions of dollars in revenue. Overall, the advisory portion of our case study required our group to have more in-depth discussions than we had previously had to find a solution that works for Pfizer.

<u>Delivery Services:</u>

During the third week of preparation for the case competition, our group acted as an advisory team. Our task was to identify and develop two strategies that Pfizer could undertake to improve its performance. In building these plans, our group investigated Pfizer’s current practices to avoid repetition, but searched across industries to potentially find a suitable application to Pfizer. Of our two strategies, one models itself after the success that delivery services bring by increasing revenues, and the other offers a suggestion for an acquisition that would allow Pfizer to capitalize on a fresh market opportunity.

Pfizer faces competition from its generic competitors that undercut them on prices of their over-the-counter medicines such as Aleve and Robitussin, among others. This low-cost competition takes away from Pfizer’s ability to raise prices as the normal costs of doing business increase due to contractual increases over time. This is a problem that Pfizer has combated with online marketing and two-day shipping guarantees for many products, but this is not enough in today’s fast-paced world. Every industry, from restaurants to grocery stores to car dealerships, is moving towards same day delivery, and in many industries, even hourly guarantees.

Companies such as Walmart and Amazon have made great headway into creating an infrastructure for this next step in customer innovation. Walmart has the ability to have a warehouse attached to each store that provides the inventory to meet the same day delivery needs. Amazon has distribution centers in several large cities around the United States including Seattle, Washington; New York City, New York; and Dallas, Texas. Totaling 27 cities that offer same day delivery, Amazon has built an excellent model to evaluate.

Pfizer does not offer nearly as many products as Amazon and Walmart do, but Pfizer can lease warehouse space that is unused to house their more limited products. Creating an efficient delivery structure is obviously the biggest challenge to this issue, but there is a model to follow. A now defunct company called HomeGrocer (later bought out by Webvan, also defunct) maintained a warehouse that contained many more items than Pfizer would be storing that required different temperature storage units and a delivery system that handled up to $1 million in sales each day at its peak.

Operating a same day delivery system would come with costs, from warehouse space to dispatchers to webhosting and delivery drivers and vehicles. At first, this may seem to accomplish the exact opposite of what it was meant to do since prices would have to be increased to afford these new expenditures, or less profit would be made, defeating the purpose.

People are more than willing to pay a premium to receive their items as soon as humanly possible. DoorDash delivery can cost as much as 30 to 40 percent more than an in-person pickup in many cases. HomeGrocer charged a hefty fee to have things delivered on the same day, and though it reached its peak in 2001, it was the largest grocery delivery service in terms of daily sales revenue until the British firm Ocado surpassed them in 2010.

Amazon and Walmart's approach to the system is low-cost leadership which would not be the angle at which Pfizer needs to approach this venture. Medicines, such as Advil and Robitussin, are items that consumers would pay greater fees to obtain if they were able to continue resting in the comfort of their homes. As Pfizer understands, when people are not feeling at their best, they are willing to pay more for extra convenience. The entire premise of this idea is that customers are willing to stay at home and pay more instead of going to the local convenience store to guarantee lower prices.

This concept has been proven time and time again by different industries branching out into delivery that at first were skeptical. Pfizer can realize great potential that its competitors have not seized upon yet. In fact, a similar venture by CVS correlated to a three percent increase in revenues. Applied to Pfizer's over-the-counter drugs, which account for around six percent of their $51.75 billion in revenue, this could represent an increase in revenue of over $93 million in the first year alone. This increase along with the three percent growth rate that the firm has been realizing, means they stand to increase revenues by approximately $495 million over the next five years from this deal.

<u>MindMed Acquisition:</u>

Mental health is not new. The attention that the public has given mental health in recent years, however, has increased significantly. Pfizer has already capitalized on the pharmaceutical side of medication for depression and anxiety through Zoloft, Xanax, and Effexor. A new market surrounding mental health is in its early inception: psychedelics. There are several companies in the process of developing potentially valuable intellectual property related to psychedelic pharmaceuticals. Many of these companies, however, do not have the infrastructure to maximize their market share in the pharmaceutical world.

An example of one such company is MindMed. They have clinical trials for several drugs using LSD and MDMA, two psychedelic compounds. Their drugs are marketed for anxiety, historically untreatable depression, and, potentially most importantly, addiction. The addiction drugs related to the opioid crisis in the United States alone had a market value of over $3 billion in 2020. MindMed also recently acquired a leading AI telehealth company, HealthMode, which would allow them to administer the accompanied mental health counseling. MindMed's total assets and debts, however, are only $28 million. Pfizer should buy MindMed. Pfizer could easily purchase MindMed with cash. MindMed currently has no revenues; they are purely research and development. They do have a high market capitalization since their stock price has rocketed in the last six months; it went from a penny stock to over the $4-mark, so the market capitalization is a fickle metric. Even a generous multiple of five would only cost $140 million; Pfizer had over $1 billion in cash on hand in 2019 that they could use to finance the acquisition.

Once they acquire MindMed, they're projected to have drugs ready for market by the end of 2023 with both of their top developments finished by the middle of 2024. Operating MindMed has historically cost $20 million a year. So, over three years, the project would cost $200 million in total. Pfizer sold over $800 million in anxiety and depression medications in 2019 alone from just three drugs. According to predictions based on the current market for depression, anxiety, and addiction medications, and Pfizer's manufacturing and marketing capabilities, Pfizer can make a return on its investment within the first couple of years with hundreds of millions in revenue being added to their books. Figure 3 below shows potential revenues resulting from the MindMed acquisition in millions of dollars.

Revenues in Millions	2024	2025	2026	2027	2028
LSD Therapy	75.00	82.50	90.75	99.83	109.81
18-MC	0.00	300.00	300.00	300.00	300.00
Total	75.00	382.50	390.75	399.83	409.81
Expenses	71.75	283.93	289.62	295.88	302.77
Profits	3.25	98.58	101.13	103.95	107.04

Assuming that each LSD therapy costs $250 and 300,000 people receive treatement the first year (0.1 Percent of the American Population) and that number grows 10 percent each year.

The 18-MC is much more scalable as an addiction pharmaceutical. At 10 percent of the market for opioid addiction alone, that would be $300 Million with room to grow in the $3 Billion market.

Expenses will be $20 Million to operate MindMed in addition to an operational percentage of 69 percent of revenues; thier operating income for 2019 was 31 percent.

Figure 3

Conclusion:

Pfizer has long been one of the largest pharmaceutical companies in the world, but every company must continue to expand their horizons to be able to compete long-term. Pursuing an acquisition of MindMed and same day delivery infrastructure in large US cities can be the ideas that keep them at the top for years to come. These two potential paths have the ability to positively impact Pfizer’s balance sheet and income statement. Risks are a given, but these two areas of expansion are looking to the future based upon what direction consumer trends are going. Holistic healing is becoming increasingly popular while delivery is seeping into every industry in the world, so Pfizer has a chance to lead their competitors into the future of pharmaceuticals.

IX - CASE COMPETITION - EPS

Completed by a group consisting of deYampert Garner, Laine Keel, James Mclemore, Jamison Russ, Cristina Trefry

Introduction:

For the fifth week of preparing for the case competition, our group worked through a financial analysis of Pfizer. Stock pricing, while not always a perfect indicator of the value of a company, is generally considered to be a fair method of valuation, especially when considered over a number of fiscal periods. Our analysis involved working with the stock price and outstanding share numbers to find the price-to-earnings ratio. In a bit of a circular problem, we then used this ratio to predict Pfizer's growth given an increase in earnings per share. These increases in earnings come from the enactment of the advisory portion of the case competition. Week four represents a more thorough quantitative financial analysis of Pfizer and how our suggestions will improve the company.

Current Stock Price and Price-to-Earnings Ratio:

Pfizer's stock's closing price on the last day of the fiscal year was $36.41. Pfizer's Earnings per Share (EPS) was $1.73. Pfizer's price-to-earnings ratio on the last day of the fiscal year was $21.05. This was computed by dividing $36.41 by $1.73. On February 24, 2021, Pfizer's stock's closing price was $33.75.

Effect on Beta:

Beta allows for a company to compare how their stock moves in relation to all other stocks in the market. Beta can be grouped in three ways: one, below one, and above one. A beta of one means that the stock's price moves with the market, and generally only the market has a beta of one. A beta of below one means a stock is less volatile and more stable than the market, and a beta above one means that stock is more volatile than the market. Many say that beta is an indicator of short-term risk rather than long-term risk. Pfizer's beta is 0.63 which means that Pfizer's stock is more stable and less volatile than the market. Pfizer has a total of 16 analysts who watch their company on a daily basis. The forecasted growth rate for Pfizer in the current year is 49.10 percent with the following year having a growth rate of (7.6) percent. Pfizer's five-year growth rate is 3.6 percent. Pfizer's buy and sell recommendation consists largely of the recommendation to hold and occasionally the recommendation of buying.

Net Income Increase:

To model the growth of Pfizer's stock, our group implemented a basic earnings multiplier valuation approach. Using the basic earnings per share and the actual stock price from 2020 gave our group insight into a realistic price-to-earnings ratio for Pfizer. Holding this valuation constant then, our stock price was exclusively contingent on our projected earnings. Earnings are a function of net income and outstanding shares. We assumed shares outstanding would remain constant, so earnings are only dependent on net income. Pfizer recently discontinued a large part of their operations in a joint venture with Japanese pharmaceutical company Mylan. The discontinuation makes historical data less predictive, but our group had enough information to make defendable assumptions about the ratio of revenues to income. From these assumptions, an increase in revenue would increase net income. To increase revenue, we modeled both dynamic efficiency increases, as well as new sales to reach a projected stock price increase of over 15 percent in five years as seen in Figure 4 below. Additionally, we modeled the cost of goods sold and other expenses that decrease the net income in a comparable manner by considering both the company's expected growth and the costs associated with our recommendations. Taking our expected strategies into account we project the company to experience a 14.6 percent increase in net income over the next five years with no expected growth in common shares outstanding.

Year	EPS	Price-to-Earnings	Stock Price
2020	$ 1.73	21.046	$ 36.41
2021	$ 1.75	21.046	$ 36.74
2022	$ 1.80	21.046	$ 37.92
2023	$ 1.86	21.046	$ 29.14
2024	$ 1.92	21.046	$ 40.47
2025	$ 2.00	21.046	$ 42.11

Figure 4

Conclusions:

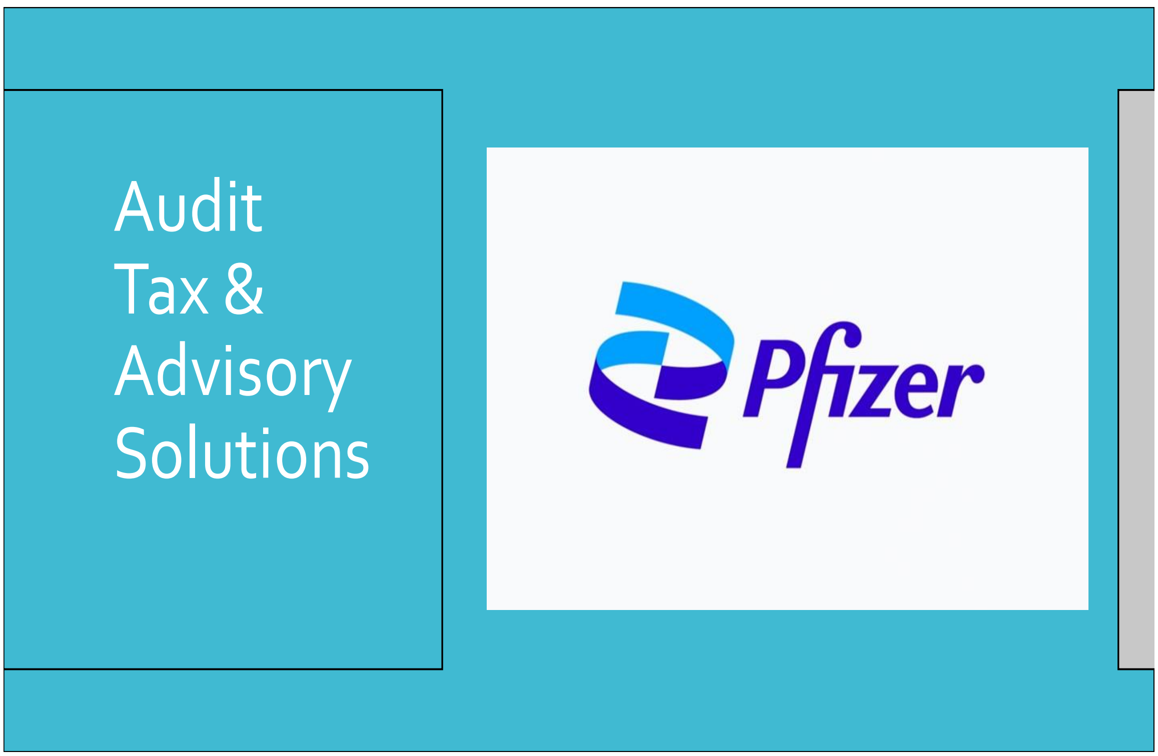
Based on the calculations done in the preceding, we believe that our recommendations for Pfizer's business and tax strategy are both valid and profitable.

First, we see a modest but respectable two percent increase in our expected return on assets over the next five years. This means that the company will become stronger and more profitable based on our suggested action. Also, we expect Pfizer to experience a 15.7 percent increase in stock price over the same time horizon. This is greater than the 12.2 percent increase they have realized over the past five years, and we believe this is attributable to the substantial increase in net income related to our suggested actions. Consequently, Pfizer will encounter some risks associated with our suggestion, but these risks should be minimal. Since Pfizer is such a large and diversified company, the beta is not expected to increase in any significant way, meaning Pfizer's stock will remain less volatile than the market as a whole.

This case allowed for our group to gain an overall better understanding of Pfizer's place in the market, and we were pleased, but not surprised to find that Pfizer has a solid place in the market. Our group faced challenges in trying to project future stock with only data from 2019. We were able to find a consistently growing stock when Pfizer's 2020 10-k was published last week. This allowed for our group to find a stronger prediction for the next five years and one that grew as well. Many of us just finished learning EPS in intermediate, so the experience of learning how to apply EPS in a more real-life setting has been beneficial. This portion of the case also allowed us to gain another layer of understanding of how our strategies we will be presenting will possibly affect Pfizer. This case allowed for our group to gain a better understanding of the market, Pfizer's said place in market, and how our solutions will turn into a positive for Pfizer's stock.

X - CASE COMPETITION PRESENTATION

Completed by a group consisting of deYampert Garner, Laine Keel, James Mclemore, Jamison Russ, Cristina Trefry



Outline

- Audit Solutions
  - Revenues
  - Goodwill
  - Accumulated Other Comprehensive Loss
  - Long-Term Debt
  - Research & Development
- Tax Solutions
- Advisory Solutions
  - MindMed
  - Same Day Delivery
- EPS & Further Analysis

Audit Solutions

Revenue

$'s in Millions	2020	2019	2018
Revenues	41,908	41,172	40,825
Revenue Reductions	13,739	12,290	10,854
Gross Revenue	55,647	53,462	51,679
Reductions as a Percent of Gross Revenue	24.69 %	22.99 %	21.00 %

Types of Reductions & Respective Solutions

Chargebacks

Rebates

Allowances

Goodwill

Figures in Millions	2020	2019	2018 (Pre-Mylan Merger)
Goodwill	$49,577	$48,202	$53,411
Goodwill Impairment	$0	$0	$0

Regression Analysis of Free Cash Flows + New Goodwill Impairment Testing Standard = More Accurate Impairment Testing

Long-Term Debt

In Millions	2020	2019
Long-term debt	$37,133	$35,955

- Risk: Completion
- Segregation of Duties
- Re-perform processes and recreate journal entries

Accumulated Other Comprehensive Loss

- Pension Plan
- Data Analytics

	2020	2019	2018
Foreign Currency Adjustment	(5,321)	(5,952)	(6,075)
Actuarial Losses	(6,507)	(6,257)	(6,027)

Research & Development

	2020	2019	2018
R&D	9405	8394	7760
R&D from Collaboration Partners	(192)	104	162

Risk

- Regulatory Issues
- Removal of Funds

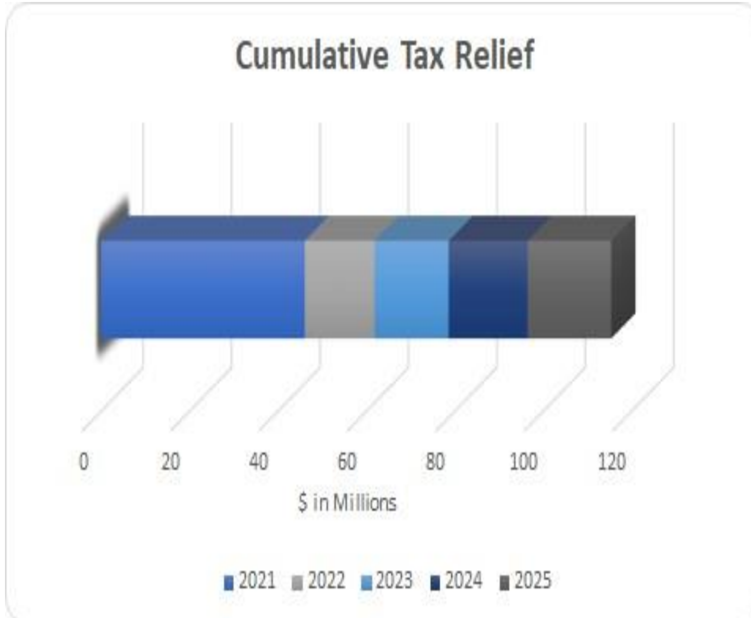
Data Analytics

- Transparency
- Less Risk

Tax Solution

Assumptions

- GILTI Rate is 10.5%
- A high first year Investment
- A constant Income exclusively from royalties



Advisory Solutions

Same Day Delivery Service

Same Day Delivery For Over-The-Counter Medicines

Revenues		Expenditures	
Delivery Fee Structure	Product Based Fee Structure	Warehouse Space & Infrastructure	Delivery Personnel
Advertising Fees & Database	Potential Test Markets	Dispatchers (automation)	Advertising

Profits

Delivery Projections in Millions for 2021

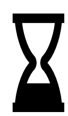
Revenues		$2,514
- CoGS		($521)
Gross Margin		$1,993
Operating Expenses		
Warehouse Space (6,000 cities, 100 pallets)	$ 108	
Delivery Infrastructure	1,052	
Dispatch Software & Processing	$ 348	
Total Expenses		$1,508
Operating Income		485
Federal Income Tax Expense (6.4%)		(31)
Net Income From Delivery Operations		**$454**

These numbers are based upon Pfizer's current Net Income as a percentage of sales. These profits could be higher if they were to make money on the delivery fee structure. We chose to present a conservative estimate for this solution.

Acquire MindMed

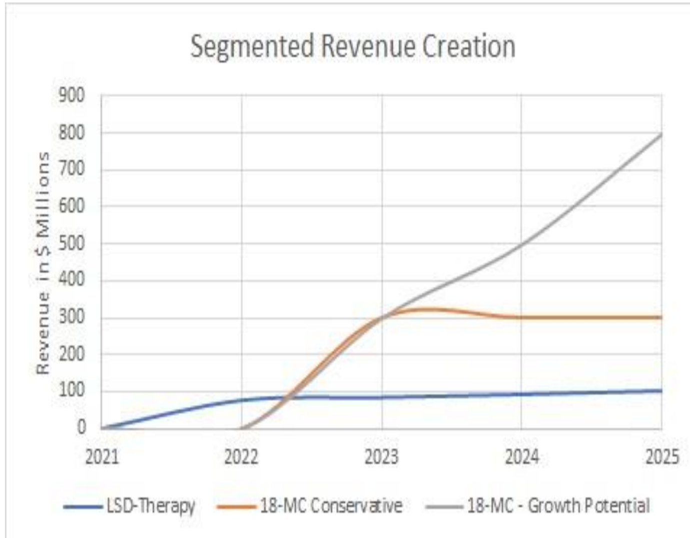
Currently developing depression, anxiety, and addiction relief medications

Offers Pfizer a new entry into to an established market

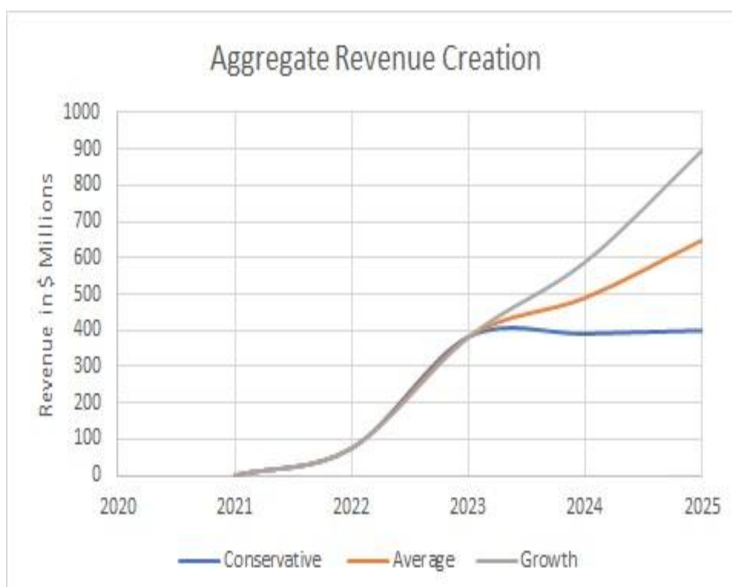


Pfizer historically utilizes M&A

What Pfizer Gets
-In Numbers-



What Pfizer Gets
-In Numbers-



What it Costs -In Numbers-

2021	Development Years	5 Year Total Cost	5 Year Profit
Acquisition Costs - No earnings - $28 Million of Debt and Assets - 5x leads to **$140 million**	Operating Costs $20 Million a year	$240 Million	$128 Million

EPS and Further Analysis

Millions of Dollars	Revenues	Net Income	ROA (OI/A)	EPS	Stock Price
2020	41,908	9,616	4.86%	1.73	36.41
2021	44,841	10,359	5.14%	1.83	38.55
2022	45,440	10,570	5.14%	1.85	38.94
2023	46,354	10,784	5.18%	1.87	39.34
2024	47,389	11,025	5.23%	1.89	39.82
2025	48,595	11,305	5.30%	1.92	40.43

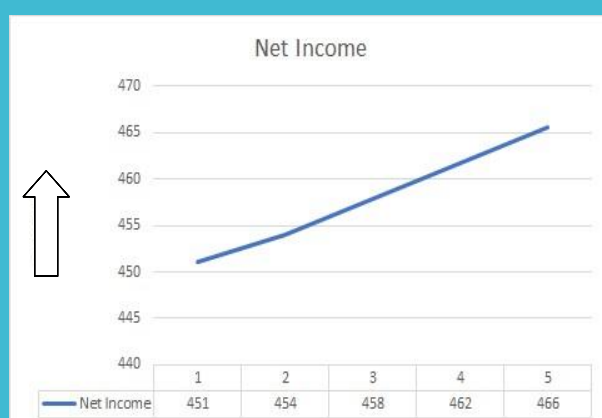
Q&A

Appendix

- Audit-Revenue
- Audit-Goodwill
- Audit-AOCL
- Audit-Debit
- Audit-R&D
- Tax Relief
- MindMed -Segmented Revenue Creation- Data
- MindMed -Segmented Revenue Creation- Graph
- Same Day Delivery Profits
- Same Day Delivery Profits Graph
- Revenue Growth
- Stock Prices & EPS

$'s in Millions	Income	Investment in Fixed Assets	Total Investment in Fixed Assets	Income applicable to GILTI	GILTI Rate	Tax Burden	Tax Relief
No Change	500	0	0	500	10.50%	52.5	0
2021	500	400	400	60	10.50%	6.3	46.2
2022	500	100	500	350	10.50%	36.75	15.75
2023	500	100	600	340	10.50%	35.7	16.8
2024	500	100	700	330	10.50%	34.65	17.85
2025	500	100	800	320	10.50%	33.6	18.9

Conservative Delivery Profit Line Graph



*In Millions

XI – FINANCIAL CRISIS ANALYSIS

Introduction:

For our final case study, we were asked to examine the effects of the 2008 financial crisis, paying specific attention to the basis of the issues that caused the crisis, its far-reaching effects on society as a whole, and how it has shaped our personal belief system. We were given a wide range of sources to examine: the 2010 documentary *Inside Job*, videos explaining the definition and effects of crony capitalism, and articles about how one bank has used its influence and trusted status to exploit investors and amass large profits over and over again. Using these sources, we endeavored to answer some important questions on this topic: how our trust in government and the institutions that were involved in the market collapse was affected by the crash; what our beliefs about our role as citizens and professionals are in the aftermath of this event; what parallels to our current situation we can identify and what we should take away from past mistakes.

I believe this case provided an insightful look into the pillars of our socioeconomic foundation and is increasingly relevant when considering our impending futures in the business world. The materials in this case study made me think more broadly about the impact of our duties in the professional field and our role in choosing our government. Though the extent of greed and corruption shown by many people in these materials is concerning, it clearly demonstrated one thing: most of this crisis was both foreseeable and preventable. This does not lessen the impact of this particular crisis, but it gives hope that, if we put in the effort and learn from our mistakes, disasters of this magnitude can be avoided in the future. This case, by showing the far-reaching effects of not questioning one simple formula, made me think deeply about the possible ramifications of not questioning our own assumptions. It also made me think critically about the level of faith we have in institutions that do not always have our best interest in mind. Overall, though aspects of this case were very disheartening, I think seeing such rattling material creates an important opportunity to reflect on our own beliefs and values, which is invaluable at this juncture in our lives and careers.

Problems:

When it struck, the 2008 financial crisis seemed like a wholly incomprehensible event. I vividly remember my father and his coworkers (members of the Public Employees' Retirement System of Mississippi) discussing the grim reality of their pensions, my mother worrying about the future of the small business where she worked, and seeing concerned people on TV addressing this event that I could only somewhat comprehend. Due in part to my youthful naivety and in part to the fact that many of the details wouldn't be known for some time, I assumed that the crisis unfolding was caused by some unforeseeable circumstances and that at least most of the people involved had acted in good faith and done everything in their power to stop this tragic incident. As I gleaned more information and learned more about the financial system, I learned just how naïve that assumption was. Even though I was already familiar with some of the major points presented in the material for this case study, seeing it all together and in such detail shook me to my core and made me question my faith in the government and our financial institutions, as well as my own role in society.

Coming into this case, my faith in government was already fairly low. Years of nothing but gridlock, hostility, and officials acting in their own self-interest had eroded my belief that these people care about anything more than personal gain or points in some political game. That being said, the information presented in the documentary *Inside Job* and the accompanying readings have lowered the bar even further. There are two major and interrelated factors from the material that reduced my confidence in government officials: the effects of big money in politics and the egregious conflicts of interest that were allowed to happen.

The influence of the big money is not new; it is present throughout the entire political system and can be seen on almost all issues. This is clearly demonstrated in *Inside Job* as well as the *Rolling Stone* article as it relates to the deregulation of the banking industry (Ferguson 2010) (Taibbi 2010). Wall Street executives and financial lobbyists spent years and millions of dollars convincing congress to haphazardly strip away any form of regulation on the financial sector, declaring that they were perfectly capable of self-regulation. These investments, in the form of campaign donations, board of director seats, and lucrative speaking engagements, paid off for Wall Street. One by one, regulations protecting the everyday people were removed, transferring more power to the banks. This is most notably seen in the passing of the Commodity Futures Modernization Act of 2000, which ensured that derivatives remained unregulated (Ferguson 2010). Despite warnings by Brooksley Born, the chairperson of the Commodity Futures Trading Commission, about the dangers of leaving these derivatives unregulated, Congress passed this legislation at the urging of the bankers (Ferguson 2010). This led to the prevalent use of credit default swaps on bonds composed of subprime mortgages. This led to immense profits on Wall Street and ultimately the colossal losses of the financial crash which the everyday people, who Congress is supposed to serve, ultimately paid for.

Next, the prevalence of officials who were allowed to conduct their duties even though glaringly obvious conflicts of interest existed also reduced my faith in the political system. As explained in the *Rolling Stone* article, a string of former Goldman Sachs executives, as well as other prominent bankers, were chosen for government positions that oversaw the operations of their former employers (Taibbi 2010). Individuals such as former Treasury Secretary Robert Rubin oversaw and helped implement the deregulation of the financial sector that had made them so much money in the past. In the same position, Hank Paulson oversaw more deregulation for his former employers and was eventually in control of distributing the bailout money back to the banks when their bad investments crashed the market. These two aren't the only former Goldman Sachs employees to obtain powerful government positions, and Goldman Sachs wasn't the only firm with alumni in power, but the fact that these two helped deregulate and then bail out their former employer exemplifies the conflicts of interest that are prevalent in government (Taibbi 2010). These examples are only on the national scale, where more people's attention is focused; this makes it truly frightening to think of how many egregious violations are happening at a smaller scale that we may never know about. These conflicts and the presence of big money in politics lead to what Joy Cost, in his video for PragerU, refers to as crony capitalism (PragerU 2016). This is where the close relationship between business and government leads to special favors and wasted tax dollars, and it is continually reducing my, and many others, faith in the government as a whole.

Today, the practices in the government are basically the same, if not worse than they were during the crisis. Big money is still prevalent in politics. It is generally accepted that most, if not all, members of congress have some ties to large corporate donors, and relaxed campaign finance rules have made this even worse over the years. Conflicts of interest still exist all around: the most recent Treasury Secretary was another former Goldman Sachs employee. Perhaps most confoundingly, policy makers are still calling for more haphazard reduction in regulations. Some of these same people were major proponents of the Commodity Futures Modernization Act of 2000, which speaks to their credibility (Ferguson 2010). Most recently, several law makers were accused of insider trading based on advanced knowledge of the extent of the Covid-19 Pandemic. All of this accompanied by a lack of transparency and accountability are further eroding trust.

Solutions:

On the brighter side, there are always innovative ideas being brought forward about how to amend some of these glaring issues and eliminate prevalent crony capitalism. Ideas such as creating blind trusts that members of congress must use to invest rather than holding individual stocks have been proposed to minimize insider trading and votes based on conflicts of interest. Additionally, measures could be taken to reduce the amount of money that is funneled into politics by wealthy corporations and other groups by adding regulations to campaign finances rules as well as lobbying. These actions would make access to lawmakers more equal and slowly help rebuild faith in the government. Also, it would cut down on crony capitalism, and reducing these conflicts of interest could prevent rulings that cause the next crisis, whatever that may be. The downside is that any of these types of reforms would have to be approved by the very people that are hurt the most by them.

Furthermore, my trust in institutions, both financial and educational, has been more thoroughly damaged by the information presented in the material than my trust in the government. Dr. David Li's Gaussian copula function is a fitting example of why the financial institutions do not deserve the amount of trust that most people have in them. This brilliant formula simplified the unfathomably complex problem of risk into one, relatively simple, equation. Bankers took this and quickly built a large part of the world's financial system around it, despite warnings from Li and others who truly understood what it meant (Salmon 2009). They saw something that produced them enormous short-term profits, and, at face value, showed no risk and ran with it (Salmon 2009). When the risks finally caught up to them, millions suffered. Did the supposed "best of the best" bankers truly not understand what was so obvious to many, or did they just not care? Either way, we should all be a lot more skeptical of people who can't even question even their most basic assumptions. If this formula were the only example of their failures, it would be enough to reduce trust in these financial institutions, but they have a long history of taking advantage of anything that will make them a quick dollar, regardless of the long-term impact. Even at times when they knew the investments they were selling were terrible, they simply tell the public that they're great investments and the people believe them (Ferguson 2010). And why wouldn't they believe the company that's worth millions? From the "investment trusts" of the Depression Era to underwriting shaky tech companies during the tech boom to the exploitation of commodities trading, these institutions flaunt rules, make millions at the expense of everyday people, and then get off with what equates to a slap on the wrist. All the while, these same institutions are still known as organizations of immense knowledge rather than organizations of immense greed.

Perhaps even more disturbing is the fact that influential institutions such as the rating agencies and even academics have helped perpetuate the lies told by the banks. Rating agencies held that the mortgage bond peddled by Wall Street deserved some of the highest ratings right up to their eventual crash (Ferguson 2010). Because of the AAA and AA ratings given by these highly trusted businesses, massive pension funds, municipalities, and individuals alike trusted that these bonds were more than the thinly veneered junk that they truly were, which is part of the reason that this crash was felt by all (Ferguson 2010). Sure, their defense that mistakes are always going to happen has some merit, but all of the agencies came to the same conclusion, despite dire warning from many sources. This calls into question whether they were all blind to such glaring risks or if they just didn't care. Whichever is true, it diminished their trustworthiness, in my eyes, to a level similar to that of a Magic 8-Ball. Additionally, members of trusted academic institutions participated in the deception that bonds were secure and that the market was stable while at the same time took home massive paychecks from Wall Street board seats (Ferguson 2010). Highly respected professors also authored complementary research about the stability of these institution and the wonderful effects of deregulation, which was paid for by the same organizations that benefited without even as much as a disclosure statement in what the movie calls “academics for hire” (Ferguson 2010). To make matters worse, none of those involved showed any remorse for these actions, which further diminished my trust in these institutions.

For these reasons, it is hard to trust the actions that these same Wall Street institutions, as well as others, are undergoing today. The recent meltdown of Archegos Capital Management because of their failure to meet a margin call is a notable example of potential issues. The firm bought massive margin calls in companies disguised as derivative contracts with leverage borrowed from some of the same banks that perpetuated the 2008 crash (Detrixhe 2021). While this isn’t anywhere near the scope of the housing market crash, the repercussions of this singular incident were felt throughout the stock market. What makes this concerning is the fact that we don’t really know how many firms are one margin call away from this level of meltdown due to the private nature of these hedge fund’s investments, according to John Detrixhe in his article in *Quartz* (Detrixhe 2021). This means that there could be many more detrimental, market shaking investments that could potentially come due.

To me, it is concerning that these institutions are still allowed to behave in the same ways that have contributed to multiple economy-wide financial downturns in the past, and many people still trust them blindly. Not only that, but people in power also still advocate for allowing them more freedom and power. For the good of the people, the opposite should be true. Sensible regulations should be put into place to ensure that these institutions can’t use their massive wealth and influence to manipulate and, frankly, steal from individuals. Not to say that all regulation is good – it certainly isn’t – but when an industry has proven repeatedly that it is only concerned with short-term profits at the expense of anyone in its way rather than the overall health of the global economy, something must be done. The regulators that oversee these firms should be strengthened so that they are able to detect these issues, and the penalties for violations should be harsh enough to discourage such reckless behavior. These giants should never be able to take advantage of an entire economy and then simply pay a fine that is only a fraction of the money they swindled from investors. Additionally, academics should, at the least, be forced to disclose their funding sources as well as any potential conflicts of interest in their work in order to prevent them from once again assisting these types of frauds. This advice is not only relevant for the financial world but also for almost everything else. Though regulation cannot prevent all disaster, it is one of our best potential defenses against wide-ranging catastrophes in the future.

Finally, this wide range of new information has made me question my own role in the greater society, both as a future professional and as a citizen. Professionally, this question is easy. The field of accounting is built on a foundation of ethics that is based in fairness and objectivity. Sure, one of our main goals as trusted advisors is to provide value to companies, but never at the expense of truth. All we have to do as individuals is keep this in mind and not stand by when faced with ethical dilemmas. Personally, I think these issues shine light on the importance of participation. Now more than ever there is a need to hold officials, elected or otherwise, professionals, and scholars accountable for their action, and it is all of our duties to do so.

Conclusion:

In conclusion, learning the full extent of the financial crisis of 2008 made me question much of the foundation of our society and my role in it going forward. While it was disheartening to see the corruption and crony capitalism that is abound in our government and the immense greed that drives some of our most trusted institutions, all hope is not lost. We as citizens hold a lot of power that can be expressed though collective participation. Hopefully, with enough organization and forethought, we as a collective can take better control of the establishment that affect our daily lives and focus them on long-term health and stability instead of short-term profits. With all of this and plenty of effort, we as a collective can certainly lessen the effects, if not prevent, of many future disasters.

XII - HONOR STATEMENT

“On my honor, I pledge that I have neither given, received, nor witnessed any unauthorized help on this thesis”

Laine Keel

Laine Keel

XIII - ADDITIONAL SIGNATURES

<u>Contemplation of Asset Concepts:</u>

"On my honor, I pledge that I have neither given, received, nor witnessed any unauthorized help on this Asset Concepts Case"

Mary Grace Gaines

Laine Keel

Olivia Meyer

Virginia Sudduth

<u>Case Competition:</u>

"On my honor, I pledge that I have neither given, received, nor witnessed any unauthorized help on this Case Competition"

deYampert Garner

Laine Keel

Cristina Trefry

James Mclemore

Jamison Russ

XIV - BIBLIOGRAPHY

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