Columbia Business School

M&A Accounting: a Practioner's Perspective, B8025, Fall 2022

Course Syllabus

I. Contact Details

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Office hours (TBD): By appointment

Teaching Assistants: TBD

II. Course Prerequisites

III. Course Description

This half semester course will explore the financial reporting aspects of an array of common M&A transactions. Companies pursue transactions for a variety of reasons, but the fundamental reason is value creation. The financial statements are the primary means through which management communicates what was acquired, how it plans to create value, and ultimately a scorecard of their success. We will discuss numerous examples to gain an understanding of how transaction motivations can drive the structure of a transaction and in turn dramatically change how it is reported. While we will touch on the perspectives of all participants in the financial reporting ecosystem at times, the primary focus is on the users of this information. Specifically, this means gaining an understanding of the information content of financial reports as it relates to transactions. Finally, we will touch on how the emerging area of ESG reporting fits into the picture. The objective is to obtain a level of literacy with respect to the accounting and reporting considerations relevant to transactions to enable the student to become an effective deal advisor.

Substantive areas covered include:

- Build vs. buy - What are the key motivations and structures and how do these manifest themselves in the information that is reported to stakeholders?
- Alliances and joint ventures - The risk-reward relationship is different than going it alone, and the impact on reported results can be significant.
- Acquisitions - We will explore adding value through financial due diligence, study purchase price allocations as tool to communicate value, and as well as the reporting implications of various M&A structures.
- Harvesting value - What are the common structures to exit a business, and what are the reporting implications for the seller and the divested business?

The focus will primarily be on strategic buyers. We will touch on the interactions with financial buyers at the various stages. While not the focus of the course, where relevant, we will discuss topical subjects such as how ESG fits in and the role of SPACs.

Topic	Class #
Build vs buy	1-2
Joint ventures and alliances	3-4
Acquisitions	5-9
Harvesting value	10-12

IV. Course Objective

The primary objective of the course is to acquire an understanding of the accounting and financial reporting aspects of various transactions that companies pursue to create value. These insights would be relevant for a participant in the M&A ecosystem.

IV. Class Schedule

First class: 9/6
Last class: 10/13
Final exam: TBA

Days	Time	Room
TU, TH	3:50 pm – 5:20 pm	Kravis 440

V. Required Reading

No textbook is required. Required readings are available on CANVAS and will consist of a compilation of articles, cases, and papers. Select podcasts and links to PwC guides as reference material will also be provided. Slides will be posted on CANVAS prior to each class. Reviewing the material in advance is required to foster robust in class discussion.

VI. Case Studies

Case #1 - Build vs. buy
Case #2 - R&D structures
Case #3 - Purchase price allocation
Case #4 - Impairment tests

VII. Grading

2 Quizzes - 10%
Class participation 30%
Group project - 30%
Take home final exam - 30%

The group project will be a 20-minute presentation to the professor and TA the week of the last day of class. The topic will be to identify an area of reporting related to deals that could be improved and how. Various approaches can be taken, e.g. thinking about the impact on an individual company, an industry, a transaction type or an area such as the accounting for intangible assets. The perspective should be that of a user of financial information. Please note that there are no shortage of academic and other proposals in the public domain on these topics, so original thought will be rewarded.

The final exam will consist of a number of fact patterns. The student will be asked to make a recommendation to management based on the facts presented. For example, how might the structure be changed to address a reporting concern that management has identified?

VIII. Course Outline

Class 1/2 Build vs Buy: After setting the strategy, management goes about either acquiring the assets it needs to execute on the strategy or develops these assets internally. We will explore how the investments companies make in these two scenarios can be very similar from an economic perspective but have a very different earnings and EBITDA profile. We will review an example that illustrates the differences in key metrics such as EPS, ROI, and EBITDA. We will also discuss the challenges that the lack of recognition of many intangible assets in the financial statements presents as well as how the rise of ESG can possibly help or exacerbate the issue.

Class 3/4/5 JVs and Alliances: Instead of going it alone, many companies chose to partner. We will discuss common business issues encountered in putting such arrangements in place, such as dispute resolution mechanisms, governance provision and compensation plans, and how they can meaningfully change key financial metrics. The type of partner, strategic vs financial, can impact the funding structure, with knock on effects on the metrics of both parties. We will translate theory into practice by analyzing an actual R&D funding structure used by companies.

Class 6 Making the buy decision (co-taught with an FDD expert): We will discuss the key elements of financial due diligence, including i) validating the value proposition through analysis of historical and projected financial data, ii) reviewing an example of a quality of earning analysis, iii) discussing the impact of aggressive historical accounting positions or errors, and iv) discussing how purchase price mechanisms tied to financial reporting metrics impact cash out of pocket. This last section will include a review of some examples of purchase price mechanisms observed in the market and illustrate how the projected ROI of the transaction is impacted by successfully navigating these provisions. These mechanisms typically have a strong grounding in financial reporting related to accrued expenses and other areas whose importance is understood by the savvy deal professional.

Class 7/8/9 Acquisitions: M&A is often the most significant investment a company will make. Given the wide array of transaction structures, the impact of the go forward financial metrics of a company can be quite complex. As a baseline we will walk through an example of a strategic acquisition. This will include reviewing a detailed example of a purchase price allocation (i.e., a disaggregation of the purchase price into the individual assets purchased. The focus here is on the information content of this exercise. We will discuss some of the common issues in M&A reporting including: i) common transaction complexities such as contingent consideration (types and why these mechanisms are used, ii) compensation structures, and iii) restructuring charges.

We will discuss an example of a private equity transaction in order to highlight how it differs from a strategic acquisition. In particular, we will review an example of so-called Black Line financial statements. We will touch on what is different about cross-border transactions and SPACs. The importance of reporting is evident from the strong correlation between SPAC activity and new SEC guidance on SPAC reporting matters.

We will discuss goodwill. The S&P 500 has several trillion dollars of goodwill. So, what does it represent, is it more than just synergies and should it be amortized? The discussion around goodwill is a good entry point into the question of how much should people focus on the earnings impact of M&A is needed given the rise of non-GAAP reporting in earnings releases.

Finally, we will discuss some of the implications post deal, for example, the impact on segment reporting and what impairments tell us.

Class 11/12 Harvesting value: While the base case is to operate the acquired assets and realize synergies and other sources of value, companies need to continuously consider whether are the optimal owner of these assets. We will discuss some of the numerous mechanisms to unlock value that have a different impact of financial metrics of the company. These include:

- Spin-offs
- Split-offs
- Sale
- Contribution of a business to a joint venture
- Admitting a minority investor

While the impact on the company's financial metrics is important, the ultimate objective is to maximize the value of the assets or business that is being monetized. This requires the preparation of separate F/S for the business in question (i.e., carve-out financial statements). We will work through an example of such financial statements. We will discuss the key inputs and gain an understanding from both the perspective of the company as well as prospective investors.

Group project: The broad objective of financial reporting is to provide an accurate reflection of the underlying economics. This sounds straight forward yet can be complicated in the real world. Financial reporting related to significant investments often is not a good reflection of the underlying economics. In a small group, pick a transaction for which the current GAAP accounting treatment is not optimal from the perspective of deal professionals. Devise a proposal for how you would improve the accounting treatment. What are the pros and cons of this proposal?