Department of Accounting

College of Commerce

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Financial Accounting

Ph.D. Qualification Examination

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PART I – 50%

(1) In 2002, the European Union (EU) Parliament passed a regulation that requires consolidated and simple accounts for all companies listed in the EU to use International Financial Reporting Standards (IFRS) for fiscal years starting after January 1, 2005. This change in accounting systems will have a large impact on the information environment for EU companies. From academic perspective, one issue naturally raise as to how mandatory adoption of IFRS in the European Union affects financial analysts' behavior? Please **briefly** present a proposal on this issue, including topic, hypotheses, and research design. In addition, please use difference-in-difference method in your research design. (17)

(2) Methodology:

2.1 Voung Test

(a) What is the Voung test?

(b) In what situation Voung test may be applied in accounting literature? Please cite literature to illustrate your points. (8)

2.2 Level and change model

(a) What is the difference between level and change models?

(b) In what situation these two models may be applied in accounting literature? Please cite literature to illustrate your points. (8)

(3) Manufacturers who provide product warranties are required to accrue a warranty expense at the time of sale. Like many other accruals, warranty expenses are estimated based on company's projections of future claims. Warranty expenses are an important selling expense and can be substantial.

The disclosures of warranty expenses and liabilities were voluntary until the issuance of FIN 45 - *Guarantor's Accounting and Disclosure Requirement for Guarantees, Including Indirect Guarantees of Indebtedness of Others* in 2002 (FASB 2002). By mandating disclosures, FIN 45 expands the information made available to investors about firms' warranty accruals, claims, and liabilities. Beginning in 2003, firms provide: (1) the estimated amount of future payments under the warranty plan (warranty liabilities), (2) the accounting policy and methodology used in determining warranty liabilities, and (3) a tabular reconciliation of the changes in the warranty liability for the reporting period. This reconciliation presents the beginning balance of the warranty liability, the reductions in that liability for payments made under the warranty plan (i.e., claims), the changes in the liability for accruals (i.e., warranty expenses) related to product warranties issued during the reporting period, the changes in the liability for accruals related to preexisting warranties (including adjustments related to changes in estimates), and the ending balance of the warranty liability.

According to the above statements, what topic you can do? Please **briefly** present a proposal on this issue, including topic, hypotheses, and research design. (17)

Appendix A provides two examples of warranty disclosures from the financial statements of Dell and Western Digital.

Appendix A

Sample warranty disclosures

Dell Corp.

		Fiscal Year Ended (in millions)	
	February 1, 2008	February 2, 2007	February 3, 2006
Warranty liability:			
Warranty liability at beginning of year	$ 958	$ 951	$ 722
Costs *accrued* for new warranty contracts and changes in estimates for pre-existing warranties [a]	1,141	1,242	1,391
Service obligations honored	(1,170)	(1,235)	(1,162)
Warranty liability at end of year	$ 929	$ 958	$ 951
Current portion	$ 690	$ 768	$ 714
Non-current portion	239	190	237

(a) Changes in cost estimates related to pre-existing warranties are aggregated with accruals for new warranty contracts. Dell's warranty liability process does not differentiate between estimates made for pre-existing warranties and new warranty obligations.

Western Digital

Product Warranty Liability

Changes in the warranty accrual for 2008, 2007 and 2006 were as follows (in millions):

	2008	2007	2006
Warranty accrual, beginning of period	$ 90	$ 89	$ 92
Charges to operations	106	74	76
Utilization	(73)	(52)	(49)
Changes in estimate related to pre-existing warranties	(9)	(21)	(30)
Warranty accrual, end of period	$ 114	$ 90	$ 89