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Personal Finance

Cutting Through Form 10-Qs

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5/13/2006 1:20 PM EDT

URL: <http://www.thestreet.com/university/personalfinance/10285453.html>

Between Mother's Day, Father's Day, May weddings and June graduations, it's hard to keep coming up with gift-giving ideas.

So instead of just cutting your loved one a check, how about giving a few shares of stock in really solid company? And since most companies' quarterly reports, formally known as 10-Qs, have recently come due to the **Securities and Exchange Commission**, all the info you need to make a good choice is readily available.

The 10-Q is a mini-version of the 10-K, otherwise known as the annual report. It's basically a financial report that details what happened to a specific company over the last three months. So if you put money in a publicly traded company, then you should read its 10-Q, says Dan Noll, director of accounting standards at the American Institute of Certified Public Accountants.

You can find these filings online at the SEC's Web site. There's some important stuff in there you should know about.

Avenue Q

The 10-Q is an unaudited document that the SEC requires public companies to file. It's a comprehensive report of the company's performance, due 35 days after each of the first three fiscal quarters. (There is no filing after the fourth quarter because that is when the 10-K is filed.) So the multitude of companies whose first quarters ended March 31 should have filed their reports in the past few weeks.

In the 10-Q, you'll find financial statements, a summary discussion from management, and some detail on the "material events" that may have occurred during the period -- like stock splits or acquisitions.

Get Your 'Street Feet' But realize that this document is unaudited. That means the company's auditors don't have to even look at it. Many auditors will review it to make sure there are no gross mistakes, says Ed Ketz, an associate professor of accounting at Penn State University. But the auditors don't have to provide a formal opinion like they do with the annual report.

To view Tracy Byrnes' video take on 10Qs, [click here](#).

Still, you can learn a lot about your company from its 10-Q.

Probably the best place to start is the section called "Management's Discussion and Analysis," or MD&A. This summary details the company's results and analyzes its current outlook. Anything out of the ordinary that happened should also be detailed here. There may have been industry issues or a company catastrophe. So read it carefully -- but be skeptical. A rain storm might be catastrophic to a tobacco crop, but if your company

tries to blame a drop in sales at its retail store on excessive rain storms, you have to wonder where everyone's umbrellas were.

Number Crunch

Every 10-Q should include an income statement, balance sheet, and cash flow statement. Each are worth a look.

- **Income Statement:** Be sure to examine the revenue number on the income statement, says Eric Heyman, senior vice president, director of research for the Olstein Financial Alert fund.

Revenue represents the money the company collected for any goods provided and/or services performed. Clearly, you'd like to see an increase in revenue over the last quarter, but if your company has seasonal sales, you might not. A better comparison would be to look at revenue from the same time last year.

And that's exactly why you can't read your company's 10-Q in isolation, warns Heyman. The numbers have no meaning if you have no basis of comparison.

So find the percentage difference from the current quarter's revenue balance to the same quarter last year. Big percentage changes relative to past performance should be red flags.

But how can you tell if the percentage change is big or just normal? Go back to the MD&A. If a percentage is abnormal, management should've addressed it.

In addition, compare against a competitor. Big percentage changes from one year to the next may be standard for the industry. Or there may have been an industry reason for the big swing.

- **Balance Sheet:** Move on to the balance sheet. Depending on your company's industry, some of your bigger concerns should be with its accounts receivables and debt, says Heyman.

If a sale is made on credit, a corresponding "receivable" account will be created on the day of that sale. So the accounts receivable balance is the total money owed to the company by the customer as a result of sales. And you want to know that your company is properly collecting on the money it's owed.

Again, do a quarter-to-quarter and year-over-year comparison yourself.

Same goes for debt. If debt levels are going up, figure out what financial obligations are coming due. You should've read that in the liquidity section of the MD&A, but you might need to go back and refresh your memory.

Then flip to the footnotes. That's the text that comes after the financial statements in the 10-Q. There's always a footnote that addresses the company's debt responsibilities, so make sure it all seems copasetic to you.

- **Cash Flow Statement:** The cash flow statement is arguably the most important statement in the whole document but, unfortunately, it can also be one of the most confusing.

But it tells you what the company has been doing with its cash and how much it has left for the future. Remember, cash is king, so if you see "red" on this page, be skeptical.

Here's a down-and-dirty way to way to figure out your company's cash standing though: Subtract "cash from investing" from "cash from operations," suggests Ketz.

The higher the number, the better. Again, do prior-quarter and prior-year comparisons.

More Help is on the Way

While we by no means tackled everything, you should now at least have a clue about walking through a 10-Q.

But if some things are still confusing you, then get on the phone and call investor relations, suggests Ken Jenke, chairman at National Association of Investors Corp. "That's why they've got toll-free numbers. They're supposed to give individual investors attention too."

And stay tuned. Over the next few weeks, we're going to dive deeper into each of the financial statements and really help you perform your own mini-audit.



Because, let's face it, if your hard-earned money is in management's hands, you owe it to yourself to understand what they're doing with it.

Tracy Byrnes is an award-winning writer specializing in tax and accounting issues. As a freelancer, she has written columns for wsj.com and the New York Post and her work has appeared in SmartMoney and on MarketWatch. Prior to freelancing, she spent four years as a senior writer for TheStreet.com. Before that, she was an accountant with Ernst & Young. She has a B.A. in English and economics from Lehigh University and an M.B.A. in accounting from Rutgers University. Byrnes appreciates your feedback; [click here](#) to send her an email.
