Preface

Most firms represent businesses. The language of business is finance. Therefore, the lawyer who has a practical working knowledge of financial concepts, terminology, and documents has a significant advantage over those who don’t. That skill will be valuable in many contexts, such as handling the sale or purchase of a company or business, negotiating a loan agreement, preparing or reviewing disclosure documents, and handling securities cases and cases where the measurement of damages is involved.

Some readers will find this book very readable. We hope that many of you will count yourselves among this group. For those who find this book challenging, we hope that you will at least be able to gain an increased understanding of the basics of accounting and finance. We also hope that you will not be discouraged if this material does not seem intuitive to you. You are in good company, and many have found that understanding comes with familiarity.

Some will read the book straight through, though we recognize that some of you will not. (It is far easier to put down than your favorite novel!) Either way, we hope that you will find it useful to refer to this book and read the relevant passages that relate to work that you are performing for your client.

This is the third edition of this book. We hope that we have improved it each time, but must confess that the rules and concepts that we have tried to capture have continued to become more complex and that has presented a challenge, as we try to do these topics justice, while making the book readable. For example, the convergence of U.S. and international accounting rules (GAAP and IFRS) has made great strides in recent years, driven by the globalization of the capital markets, and has caused rule makers to rethink some of the basic rules of accounting. In some areas, you will find that the rules are so complex that a full treatment of them is beyond the scope of this book. In those cases, we have tried to provide you with a conceptual overview and the key structure and elements of the rule so as give you what you need to know in 90 percent of the situations you will run into and the foundation to understand the other 10 percent if you ever need to.

We also believe that the importance of the topics covered in this book for any practicing business lawyer has grown with the complexity of the material. As the capital markets have become more efficient and global in nature and as the science of management has become more sophisticated, companies are increasingly challenged to meet the performance expectations of their shareholders. Stated simply, the low-lying fruit has largely been picked! Management of those
companies seeks new ways to create value and will welcome legal counsel who can play a role in that value creation.

Of course, to play that role requires a basic understanding of how a company (and the markets) measures performance, as well as some of the opportunities and pitfalls that your client is likely to face as it tries to improve that performance. Our objective is to increase your understanding of those factors.

Chapters 1 through 6 are intended to provide a basic overview of the content and purpose of financial statements and the rules by which they are prepared. Chapters 7 and 8 provide some insight as to how you might analyze those financial statements to learn about the performance of the companies they describe.

The content of Chapters 1 through 8 focuses on understanding financial statements and hopefully will teach you how to understand what they are telling you. Beginning with Chapter 9, the book delves into topics more common to the study of finance. Chapters 9 through 16 explain the building blocks used in valuing companies. In Chapter 17 we explore cases where the shares held by different shareholders in the same company may be valued differently. We then explore the M&A process in Chapters 18 and 19, both from the perspective of a company’s M&A strategy (Chapter 18) and by exploring ways that legal counsel might add value to the process (Chapter 19). The final substantive chapter is Chapter 20, which discusses some strategies that a company might explore to enhance its performance. Because this chapter draws on a number of the concepts discussed in previous chapters, it is in some ways a capstone chapter. We conclude with some final thought in Chapter 21.

There is a vast range in the financial sophistication of lawyers, from rank neophyte to highly savvy and skilled. Wherever you fit on that spectrum, we hope that you will find this book useful, whether you read it from start to finish, use it as a reference resource, or both.

The ability to work with financial and accounting matters is like learning a foreign language. The first time one looks at a balance sheet, income statement, or cash flow statement, it looks like it may as well be written in Farsi or Chinese characters. Eventually you can become, as some people do, as comfortable with the numbers as you are with words. We say that mindful that many lawyers are basically allergic to numbers and glaze over at the very thought of them. If you are one of them, you can focus on the concepts in this book, though it will be hard to avoid numbers altogether. Some good news is that there is virtually no difficult math. At times being able to add, subtract, multiply and divide will be a plus, but that’s about it. There is some basic algebra, but nothing a sixth grader couldn’t do.

We hope that reading this book will do for you what it did for one of our clients, who told us that this knowledge not only makes the lawyers in his firm 10 percent more effective all the time but also reduces the risk of a massive mistake that would cost a client and his firm much in dollars and reputation. Further, we hope that by enabling you to work at a higher level it will make the practice of law more enjoyable for you.

Robert B. Dickie  
Peter R. Russo