

Our 10-K Cheat Sheet: How to Speed Read a Company's Annual Report

Make short work of a long form by focusing on these seven points.

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From *Kiplinger's Personal Finance* magazine, May 2011

It's like Silas Marner -- long and boring and nobody wants to read it. But if you're a serious investor, you need to review a company's Form 10-K. The 10-K is an annual summary of operations required by securities regulators. "It's where the buck stops," says David Brady, a Geneva, Ill., money manager. "There's no sugarcoating. No hype. Just what the company does, its products and how it makes money."

The good news? You don't have to read every word. In fact, smart investors focus on a few key sections for red flags -- and skim the rest.

(Also see our [8 Outrageous Executive Perks slide show](#) to learn what you can find by studying a company's proxy statement.)

Stock Classes

Where to find it: The opening page.

Why it's important: If there are multiple classes of stock -- Class A, B and so on -- it may mean that a minority of shareholders controls the company. Suppose you want to buy the stock because you think the company is a takeover target. Be aware that if the dominant holders are against the deal, an acquisition is unlikely.

Auditor Changes or Disagreements

Where to find it: Middle of part II.

Why it's important: If the company has changed auditors or says it disagrees with its accountants, that's a warning that you may not be able to trust the numbers.

Auditor's Report

Where to find it: Near the end or in the notes.

Why it's important: When auditors question a company's ability to stay in business, you're in the investment-risk red zone. Instead, you want to see boilerplate: that the auditors say the financial statements accurately represent the company's financial position.

Risk Factors

Where to find it: Middle of part I.

Why it's important: Most of this is standard stuff -- for example, stocks are volatile and some businesses are seasonal. Look for anything out of the ordinary, such as "our top 15 customers account for approximately 80% of our net sales," or "numerous product-liability suits have been filed against us" -- real warnings in the latest 10-K of Matrixx Initiatives, a maker of over-the-counter drugs. Or consider the language in the 10-K filed by Live Nation Entertainment (symbol [LYV](#)), the concert promoter and owner of Ticketmaster.com: "We have a large amount of debt and lease obligations that could restrict our operations and impair our financial condition."

Legal Proceedings

Where to find it: Near (and often related to) "risk factors."

Why it's important: A certain amount of litigation is to be expected, especially for a big company. Look for lawsuits that the company says could have a "material" impact on earnings -- good or bad.

Consolidated Financial Statements

Where to find it: Near the end or in the notes.

Why it's important: Look for rising sales, net profits and cash flow. If you saw a red flag in the "risk factors" section, ferret out the details here. With Matrixx, for example, it turns out that 51% of its sales come from just three customers.

Management's Discussion of Results

Where to find it: Beginning of part II.

Why it's important: This is the bosses' unvarnished explanation of what has happened in the past year and the company's prospects. If something about the firm's finances struck you as strange -- cash flow is evaporating or sales have stalled -- this section should tell you why and whether the problem is permanent or temporary.

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