Student name:\_\_\_\_\_\_\_\_\_\_

1. As finance emerged as a new field, much emphasis was placed on mergers and acquisitions.

* true
* false

1. Inflation is assumed to be a temporary problem that does not affect financial decisions.

* true
* false

1. Financial capital is composed of long-term plant and equipment, as well as other tangible investments.

* true
* false

1. Real capital is composed of long-term plant and equipment.

* true
* false

1. During the 1930s, financial practice revolved around such topics as the preservation of capital, maintenance of liquidity, the reorganization of financially troubled corporations, and bankruptcy.

* true
* false

1. In the mid 1950s, finance began to change to a more analytical, decision-oriented approach.

* true
* false

1. Recently, the emphasis of financial management has been on the relationship between risk and return.

* true
* false

1. The first Nobel Prizes given to finance professors were for their contributions to capital structure theory and portfolio theories of risk and return.

* true
* false

1. How investors handle risk is an important topic that usually only economists observe.

* true
* false

1. Mortgage-backed securities were devalued by accounting standards because of the high credit ratings (AAA).

* true
* false

1. "Credit default swaps" are one of several tools that Congress and the President of the United States have jointly developed to ease the financial crisis that began in 2008.

* true
* false

1. The Dodd-Frank Act was created by Congress along with its goals and regulatory responsibility, but it is facilitated by various agencies.

* true
* false

1. The difference between investments and corporate finance is that investors use investment principles to value the stock and bonds of many companies whereas corporate finance principles are used to determine which assets the firm should develop or buy, which securities to issue, how management compensation should be structured and other inside of the company issue.

* true
* false

1. The Dodd-Frank Act contains the Volcker Rule, which encourages financial institutions to allow for more speculative investments for average investors.

* true
* false

1. The Dodd-Frank Act's oversight allowing regulation of banking fees and available products has been considered as not being in the best interests of a free market.

* true
* false

1. The Internet impacts e-commerce by creating a mechanism for improved communications between a business, its customers, and its suppliers.

* true
* false

1. The Internet is responsible for many new business models.

* true
* false

1. Businesses will increasingly rely on B2B Internet applications to speed up the cash flows through their firms.

* true
* false

1. Sole proprietorship means single-person ownership and offers the advantages of simplicity of decision making and low organizational and operating costs.

* true
* false

1. Under the 2017 Tax Cuts and Jobs Act, the most significant change is that the corporate tax rate goes from 35 percent to 21 percent, which puts U.S. Companies on competitive footing with many other countries.

* true
* false

1. With more employees working online, company headquarters and operations for most multinational companies can be placed almost anywhere. In response, countries around the world have slashed tax rates in an effort to attract and retain new businesses.

* true
* false

1. Profits of sole proprietorships are taxed at corporate tax rates.

* true
* false

1. Sole Proprietorships, partnerships and limited liability partnerships are considered pass through forms of organizations because the income passes through to the owners and is taxed at the owner's individual tax rate.

* true
* false

1. To reduce the burden on small firms, the government established a 25 percent deduction of qualified business income from pass through businesses.

* true
* false

1. There is unlimited liability in a general partnership.

* true
* false

1. A limited partnership limits the profits partners may receive.

* true
* false

1. In terms of revenues and profits, the corporation is by far the most important form of business organization in the United States.

* true
* false

1. As noted in *Finance in Action*, initial public offerings have now increased because long-term results are favored by shareholders and institutional investors.

* true
* false

1. Dividends paid to corporate stockholders have already been taxed once as corporate income.

* true
* false

1. One advantage of the corporate form of organization is that income received by stockholders is not taxable since the corporation already paid taxes on the income distributed.

* true
* false

1. A corporation must have more than 100 stockholders to qualify for Subchapter S designation.

* true
* false

1. Profits of a Subchapter S corporation are taxed at corporate tax rates.

* true
* false

1. The formation of a Subchapter S corporation is a way to circumvent the double taxation of a small corporation.

* true
* false

1. Corporate governance issues have become less important to the financial community during the first decade of the new millennium.

* true
* false

1. Agency theory examines the relationship between companies and their customers.

* true
* false

1. Institutional investors have had increasing influence over corporations with their ability to vote with large blocks of stock and replace poorly performing boards of directors.

* true
* false

1. Agency theory assumes that corporate managers act to increase the wealth of corporate shareholders.

* true
* false

1. The Sarbanes-Oxley Act reduced agency conflicts by giving corporate managers greater flexibility to select their preferred candidates to the board of directors.

* true
* false

1. A major focus of the Sarbanes-Oxley Act is to make sure that publicly traded companies accurately present their assets, liabilities, and income in their financial statements.

* true
* false

1. The Sarbanes-Oxley Act is primarily intended to increase public scrutiny of private companies that had previously been exempt from many public disclosure requirements.

* true
* false

1. Timing is not a particularly important consideration in financial decisions.

* true
* false

1. The higher the profit of a firm, the higher the value the firm is in the market.

* true
* false

1. There are some serious problems with the financial goal of maximizing the earnings of the firm.

* true
* false

1. Maximizing Shareholder wealth can be difficult due to daily fluctuations in stock value in combination with changing investor expectations.

* true
* false

1. Maximizing the earnings of the firm is the main goal of financial management.

* true
* false

1. The ultimate measure of performance is not what the firm profits, but how the profits are valued by the investor.

* true
* false

1. Because socially desirable goals can hinder short-term profitability in many instances, managers should avoid pursuing these goals.

* true
* false

1. Insider trading involves the use of information not available to the general public to make profits from trading in a company's stock.

* true
* false

1. If an investor hears of a large change that a company is going to make through a news article and reacts quicker than any other investor, it is considered insider trading.

* true
* false

1. When an investor has the ability to control how the stock price changes, that is considered insider trading.

* true
* false

1. Social responsibility and profit maximization are synonymous.

* true
* false

1. Irrational exuberance is when companies have stock that is undervalued.

* true
* false

1. Financial markets exist as a vast global network of individuals and financial institutions that may be lenders, borrowers, or owners of public companies worldwide.

* true
* false

1. Money markets refer to those markets dealing with short-term securities having a life of one year or less.

* true
* false

1. Money markets refer to markets where excess corporate cash is exchanged for foreign currencies that can earn a higher return than domestic money.

* true
* false

1. Capital markets refer to those markets dealing with short-term securities that have a life of one year or less.

* true
* false

1. The primary market includes the sale of securities by way of initial public offerings.

* true
* false

1. When a company is looking to raise money through issuing more shares of stock, that is considered in the secondary market.

* true
* false

1. High-quality initial public offerings are usually sold in a primary market, such as the New York Stock Exchange. However, low-quality stocks must usually be sold in secondary markets, such as NASDAQ.

* true
* false

1. Although NASDAQ is a secondary market, some of the firms traded there, such as Microsoft, are large enough to move to the primary market if they so desire.

* true
* false

1. The secondary market characteristically has had stable prices over the past 20 years.

* true
* false

1. In the United States, stocks traded on either the New York Stock Exchange or NASDAQ are considered sold in the primary market.

* true
* false

1. New issues are sold in the secondary market.

* true
* false

1. Existing securities are traded in the secondary market.

* true
* false

1. Many companies have cross-listed their stock on multiple international stock exchanges and more than several hundred foreign companies have listed their shares on the New York Stock Exchange.

* true
* false

1. Higher returns always induce stockholders to invest in a company.

* true
* false

1. Higher return means that the public company has lower risk.

* true
* false

1. Social responsibility is an expense and thus should be avoided by financial managers because it will lead to loss of income.

* true
* false

1. Financial management requires both short-term activities as well as long-term planning such as raising funds.

* true
* false

1. One of the primary disadvantages of maximizing shareholder value is that it only provides a short-term perspective.

* true
* false

1. If a company has a written code of ethics, it will assist in avoiding ethical problems.

* true
* false

1. Risk management will be an important factor over the next decade.

* true
* false

1. With the creation of Internet trading, trading through brokers became less desirable for some investors due to the higher cost.

* true
* false

1. Time value of money is the idea that a dollar received today is worth less than a dollar that we expect to receive at some date in the future.

* true
* false

1. The relationship between future value and present value is given by the following formula:  
   formula3.mml  
   FV = future value  
   PV = present value  
   i = interest rate  
   n = number of periods

* true
* false

1. Which of the following did not contribute to the financial crisis?

Solid credit ratings from the ratings agencies

The extension of credit to high-risk borrowers

The merger of JPMorgan Chase and Bear Stearns

All of the options contributed to the financial crisis.

1. Credit default swaps are

an insurance product designed to protect financial institutions from customers who default on their loans.

securities with a maturity of less than one year.

the result of a leveling off or slowing down of stock price increases.

market trades in previously issued securities.

1. What should be the primary goal of financial management?

Increased earnings

Maximizing cash flow

Maximizing shareholder wealth

Minimizing risk of the firm

1. In the past, the study of finance has included

mergers and acquisitions.

raising capital.

bankruptcy.

All of the options

1. Professor Merton Miller received the Nobel Prize in Economics for his work on

dividend policy.

investment theory.

working capital management.

capital structure theory.

1. Notable recipients of the Nobel Prize in Economics have been recognized for their contributions to the

options pricing model.

theories of working capital management.

theories in measuring risk along with return on securities.

theories of international capital budgeting.

1. Behavioral finance is the study of

how investors react to accounting-based profit fluctuations.

how investors react to interest rates and foreign currency fluctuations.

how investors react to certain ways to diversify a portfolio.

how investors react to the amount of risk versus the amount of return in securities.

1. Which of the following is NOT addressed by the Dodd-Frank Act?

Liquidation of non-bank financial companies such as insurance companies.

Identifies systematic risk of U.S. financial system.

Written certifications of financial statements by the CEO and CFO.

Registration of hedge funds with the SEC.

1. Proper risk-return management means that

the firm should take as few risks as possible.

the firm must determine an appropriate trade-off between risk and return.

the firm should earn the highest return possible.

the firm should value future profits more highly than current profits.

1. One of the major disadvantages of a sole proprietorship is

that there is unlimited liability to the owner.

the simplicity of decision making.

high organizational costs.

high operating costs.

1. One of the major advantages of a sole proprietorship is

that the owner has limited liability.

that stock in the proprietorship can be easily transferred.

that it is exempt from many tax rules that would otherwise apply when employees are hired by the firm.

low operating costs.

1. The partnership form of an organization

avoids the double taxation of earnings and dividends found in the corporate form of organization.

usually provides limited liability to the partners.

has unlimited life.

simplifies decision making.

1. A corporation is

owned by stockholders who enjoy the privilege of limited liability.

easily divisible between owners.

a separate legal entity with unlimited life.

All of the options are correct.

1. With an S corporation

income is taxed as direct income to stockholders.

stockholders have the same liability as members of a partnership.

the number of stockholders is unlimited.

the life of the corporation is limited.

1. An S corporation

is similar to a partnership in that it carries unlimited liability.

is a separate legal entity that is treated like a normal corporation.

has all the organizational benefits of a corporation and its income is only taxed once.

All of the options

1. From the 2017 Tax Cuts and Job Act, a reason to choose sole proprietorship, partnership or corporation as a form of organization is:

the number of people in the organization.

the liability of the owner.

the complexity involved with state and federal regulations and taxation.

All of the options are correct.

1. Corporate governance is the

relationship and exercise of oversight by the board of directors of the company.

relationship between the chief financial officer (CFO) and institutional investors.

operation of a company by the chief executive officer (CEO) and other senior executives on the management team.

governance of the company by the board of directors with a focus on pleasing management.

1. Many companies such as Tyco, Enron, and WorldCom that suffered financial distress in the late 1990s and early 2000s

committed fraud.

had failed corporate governance oversight.

went bankrupt.

All of the options are true.

1. Agency theory examines the relationship between the

shareholders of the firm and the firm's investment banker.

owners of the firm and the managers of the firm.

board of directors and large institutional investors.

shareholders and the firm's transfer agent.

1. Agency theory would imply that conflicts are more likely to occur between management and shareholders when

the company is owned and operated by the same person.

management acts in the best interests of maximizing shareholder wealth.

the chairman of the board of directors is also the chief executive officer (CEO).

the board of directors exerts strong and involved oversight of management.

1. Agency theory deals with the issue of

when to hire an agent to represent the firm in negotiations.

the legal liabilities of a firm if an employee, acting as the firm's agent, injures someone.

the limitations placed on an employee acting as the firm's agent to obligate or bind the firm.

the conflicts that can arise between the viewpoints and motivations of a firm's owners and managers.

1. Agency problems are least likely to arise in which organizational form?

Sole proprietorship

Limited partnership

Corporation

Subchapter S corporation

1. Institutional investors are important in today's business world because

as large investors, they have more say in how businesses are managed.

they have a fiduciary responsibility to the workers and investors that they represent to see that the firms they own are managed in an ethical way.

as a group they can vote large blocks of stock for the election of board members.

All of the options are correct.

1. The increasing percentage ownership of public corporations by institutional investors has

had no effect on corporate management.

created higher returns for the stock market in general.

created more pressure on public companies to manage their firms more efficiently.

taken away the voice of the individual investor.

1. The Sarbanes-Oxley Act was passed in an effort to

protect small business from large corporations dominating the market.

ensure that partnerships divide profits among partners in a fair manner.

guarantee that outside auditors can control corporate accounting practices.

control corrupt corporate financial behavior.

1. The Sarbanes-Oxley Act set up the Public Company Accounting Oversight Board with the responsibility for all of the following except

internal controls within companies.

controlling the quality of audits.

certifying the competence of financial executives.

setting rules and standards for the independence of auditors.

1. A financial manager's goal of maximizing current or short-term earnings may not be appropriate because

it fails to consider the timing when shareholders want increased earnings and may instead consider the manager’s own goals.

increased earnings may be accompanied by unacceptably higher levels of risk.

earnings are subjective; they can be defined in various ways such as accounting or economic earnings.

All of the options are true.

1. Maximization of shareholder wealth is a concept in which

increased earnings is of primary importance.

profits are maximized on an annual basis.

virtually all earnings are paid as dividends to common stockholders.

optimally increasing the long-term value of the firm is emphasized.

1. Which of the following is not a true statement about the goal of maximizing shareholder wealth?

It takes into account the timing of cash-flows.

It is a short-run point of view.

It considers risk as a factor.

None of the options is a false statement.

1. As mergers, acquisitions, and restructuring have increased in importance, agency theory has become more important in assessing whether

a stock repurchase should be undertaken.

shareholder goals are truly being achieved by managers in the long run.

managers are actually agents or only employees of the firm.

managers are owners of the company and act the same with the same interests.

1. Insider trading occurs when

someone has information not available to the public which they use to profit from trading in stocks.

corporate officers buy stock in their company.

lawyers, investment bankers, and others buy common stock in companies represented by their firms.

any stock transaction that violates the Federal Trade Commissions restrictions.

1. The major difficulty in most insider-trading cases has been

that lenient judges have simply released the guilty individuals.

that insider trading, even though illegal, actually serves a beneficial economic and financial purpose.

that inside trades have not been legally well-defined.

that it is hard to figure out which owner(s) benefited from the trade.

1. What is the major difference between money markets and capital markets?

One is more domestic while the other is more international.

One includes stock while the other includes loans.

The size of the profit or return on the market.

The timing of how long the security will be held onto.

1. Capital markets do not include which of the following securities?

Common stock

Commercial paper

Government bonds

Preferred stock

1. When a corporation uses the financial markets to raise new funds, the sale of securities is made in the

primary market.

secondary market.

online market.

third market.

1. Which of the following statements is not true of secondary markets?

After securities are sold to the public, they are traded in the secondary market between investors.

The secondary market prices are continually changing as investors buy and sell securities.

The sale of securities is made in the secondary market by way of a new issue.

In the secondary market, financial managers are given feedback about their firm's performance.

1. Companies that have higher risk than a competitor in the same industry will generally have

to pay a higher interest rate than its competitors.

a lower relative stock price than its competitors.

a higher cost of funds than its competitors.

All of the options are correct.

1. What is financial capital as defined in the financial industry?

The structure of the company

The sales price of stock

Profits

Money

1. The financial markets allocate capital to corporations by

reflecting expectations of the market participants in the price of the corporation's stock.

requiring higher returns from companies with lower risk than their competitors.

rewarding companies with expected high returns with lower relative stock prices.

relying on the opinion of investment bankers.

1. Corporate restructuring can be a result of more institutional ownership. Restructuring can cause

changes in the amount of assets versus the amount of liabilities of the firm.

the sale of low-profit margin divisions.

the removal of current management and/or large reductions in the workforce.

All of the options are correct.

1. A corporate restructuring can result in

changes in the capital structure.

selling of low-profit margin divisions.

the board of directors exercising control of the company’s major decisions.

All of the options are true.

1. Which of the following is not an example of restructuring?

Increase or decrease the amount of common stock.

Eliminating profitable but unrelated divisions.

Merging with companies in related industries.

Divesting of an unprofitable division.

1. Future financial managers will need to understand

international cash flows.

computerized funds transfers.

international currency hedging strategies.

All of the options are true.

1. The increase in the internationalization of financial markets has led to

companies searching the global financial markets for low-cost funds.

an increase in American Depository Receipts (ADRs) on the New York Stock Exchange.

an increase in debt obligations denominated in foreign currency on U.S. corporate balance sheets.

All of the options are true.

1. The internationalization of the financial markets has

allowed firms such as McDonald's to raise capital around the world.

raised the cost of capital.

forced companies to price everything in U.S. dollars.

All of the options are true.

1. The Internet has affected the financial markets by

creating more competition between markets.

pushing the cost of trading down.

forcing brokerage companies to consolidate.

All of the options are true.

1. Increased productivity due to technology has

increased corporations' reliance on debt for capital expansion needs.

created larger asset values on the firm's historical balance sheet.

made it cheaper (in terms of interest costs and timing of when money is transferred) for firms to borrow money.

helped to keep corporate costs in check.

1. Companies that perform well

can sell their stock for a lower price.

can minimize dilution when issuing new shares.

can issue debt at a lower interest rate.

can minimize dilution when issuing new shares and can issue debt at a lower interest rate.

1. The entity that is responsible for establishing the allocation and cost of capital is/are

the corporation.

the economy.

investors.

customers.

1. The benefits of social responsibility often include

a better reputation.

higher short-term earnings.

lower expenses.

None of the options

1. Who is accountable for social responsibility within a firm?

The board of directors

Management

Investors

The financial market

1. Regarding risk levels, financial managers should

pursue higher-risk projects because they increase value.

avoid higher-risk projects because they destroy value.

focus primarily on market fluctuations.

evaluate investors' desire for risk.

1. What is the future value of $2,000 deposited for one year earning 6 percent interest rate annually?

$120

$2.000

$2,120

$4,120

1. What is the future value of $6,000 deposited for one year earning 5 percent interest rate annually?

$6,150

$6,100

$6,300

$7,101

1. What is the present value of a $750 payment made in three years when the discount rate is 5 percent?

$646.96

$647.88

$712.50

$868.22

1. What is the present value of a $1500 payment made in three years when the discount rate is 8 percent?

$125.69

$1,190.75

$1,100.53

$1,224.22

**Answer Key**Test name: chapter 1

TRUE

FALSE

FALSE

TRUE

TRUE

TRUE

TRUE

TRUE

FALSE

Behavioral finance is something that the finance industry puts heavy emphasis on.

FALSE

These securities were devalued because borrowers defaulted on their loans and didn’t have the financial means to back up their loans in other ways.

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D

C

PV = 2000, PMT = 0, I = 6, N = 1, FV = 2120

C

PV = 6000, PMT = 0, I = 5, N = 1, FV = 6300

B

FV = 750, PMT = 0, I = 5, N = 3, PV = 647.88

B

FV = 1500, PMT = 0, I = 8, N = 3, PV = 1190.75