Corporate Finance (Canadian) 9th edition Ross Test Bank

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Chapter 02
Accounting Statements and Cash Flow

Multiple Choice Questions

1. The Statement of Financial Position is based on which following equality:
A. Fixed Assets = (Stockholder's equity + Current Assets)
B. Assets = (Liabilities + Stockholder's equity)
C. Assets = (Current Long Term Debt + Retained earnings)
D. Fixed Asset = (Liabilities + Stockholder's equity)

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

2. Assets are listed on the Statement of Financial Position in order of:
A. decreasing liquidity.
B. increasing liquidity.
C. increasing size.
D. relative life.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

3. Of the following assets, which is the generally the least liquid?
A. Marketable securities.
B. Cash.
C. Inventory.
D. Accounts receivable.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

4. Which one of these accounts is classified as a current asset on the balance sheet?
A. intangible asset
B. accounts payable
C. preferred stock
D. inventory
E. net plant and equipment

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

5. Accounting liquidity is defined as:
A. the amount of cash the firm has.
B. the turnover ratio.
C. the ability of the assets to generate income.
D. the ease and quickness with which assets can be converted to cash.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

6. Net working capital is defined as:
A. current assets plus fixed assets.
B. current assets plus stockholders' equity.
C. fixed assets minus long-term liabilities.
D. total assets minus total liabilities.
E. current assets minus current liabilities.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-03 Debt versus Equity

7. Fixed assets can be either tangible or intangible. Intangible assets are:
A. property, plant and equipment.
B. can be converted to cash in the normal course of business.
C. can be very valuable, although they have no physical presence, such as trademarks or patents.
D. are highly liquid.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-01 The Statement of Financial Position

8. Intangible fixed assets would include:
A. building.
B. machinery.
C. trademarks.
D. equipment.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

9. The primary distinction between tangible and intangible assets is that:
A. intangible assets have a physical existence while tangible assets do not.
B. intangible assets do not have a physical existence while tangible assets do.
C. since tangible assets do not have a physical existence they do not show up on the balance sheet.
D. since intangible assets do not have a physical existence they do not show up on the balance sheet.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

10. The earnings before interest and taxes, EBIT, on the income statement provides results on:
A. the post financing effect on the earnings capability of the firm.
B. the operating income for the period.
C. the gross margin of the firm.
D. the extraordinary items of the firm for the period.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-01 The Statement of Financial Position

11. In the Statement of Financial Position assets are:
A. all relatively illiquid.
B. listed at current market value.
C. listed at market value as of the most recent fiscal year.
D. listed at cost.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

12. Under IFRS the value of all the firm's assets are reported at:
A. Carrying value or market value.
B. Book value or liquidation value.
C. Market value or Carrying value.
D. Book value or Carrying value.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-02 Liquidity

13. Which of the following statements concerning the income statement is not true?
A. It measures performance over a specific period of time.
B. It determines after-tax income of the firm.
C. It includes deferred taxes.
D. It does not include depreciation.
E. It treats interest as an expense or revenue.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-02 Liquidity

14. For a firm with long-term debt, net income is equal to:
A. Pretax income - Interest expense - Taxes.
B. Dividends + Addition to retained earnings.
C. EBIT - Taxes.
D. Taxes + Addition to retained earnings.
E. Pretax income × (1 - Marginal tax rate).

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-02 Liquidity

15. Noncash items refer to:
A. the credit sales of a firm.
B. the accounts payable of a firm.
C. the costs incurred for the purchase of intangible fixed assets.
D. expenses charged against revenues that do not directly affect cash flow.
E. all accounts on the Statement of Financial Position other than cash on hand.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-02 Liquidity

16. According to IFRS, revenue is recognized as income when:
A. a contract is signed to perform a service or deliver a good.
B. the transaction is complete and the goods or services delivered.
C. payment is received.
D. income taxes are paid.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-02 Liquidity

17. The TimeNow Corporation had 2017 fixed assets of $1345, current assets of $260, current liabilities of $180 and shareholder's equity of $775. What was the net working capital for TimeNow in 2017?
A. $260.
B. $180.
C. $80.
D. $390.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-03 Debt versus Equity

18. The TimeNow Corporation had 2017 fixed assets of $1345, current assets of $260, current liabilities of $180 and shareholder's equity of $775. The 2016 fixed assets were $1300, current assets of $220, current liabilities of 300, long-term liabilities of $390 and shareholder's equity of $750. What was the change in net working capital for TimeNow in 2017?
A. 80.
B. 20.
C. 60.
D. 160.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-03 Debt versus Equity

19. Which of the following is not included in the computation of operating cash flow?
A. Earnings before interest and taxes.
B. Interest paid.
C. Depreciation.
D. Current taxes.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-04 Value versus Cost

20. _____ refers to the firm's dividend payments less any net new equity raised.
A. Operating cash flow
B. Capital spending
C. Net working capital
D. Cash flow from creditors
E. Cash flow to shareholders

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-04 Value versus Cost

21. Net capital spending is equal to:
A. net additions to Net Working Capital.
B. the net change in fixed assets.
C. net income plus depreciation.
D. total cash flow to shareholders less interest and dividends paid.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-03 Debt versus Equity

22. What is the effect on net working capital if the corporation decides to increase their investment in inventory and pay for it with cash?
A. Increase in NWC.
B. Decrease in NWC.
C. Depends on the amount of the investment.
D. No effect.
E. Depends on the amount of cash.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-03 Debt versus Equity

23. Which of the following is not a use of Net Working Capital?
A. Retirement of long-term debt.
B. Dividends.
C. Sale of equity.
D. Acquisition of fixed assets.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-03 Debt versus Equity

24. Cash flow to shareholder is defined as:
A. total cash flow from the firm plus cash flow to the bondholders.
B. repurchases of equity less cash dividends paid plus new equity sold.
C. cash flow from operations less cash flow to creditors.
D. cash dividends plus repurchases of equity minus new equity sold.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-04 Value versus Cost

25. For any individual period the firm cash flows are a circular flow of funds, this means:
A. that cash flows are always invested in fixed assets.
B. that cash flows are always in a spiral away from the firm.
C. that firm cash flows must be borrowed externally to be reinvested in the economy.
D. that all cash flows generated by the firm must equal the cash flows paid to the creditors and shareholders.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-04 Value versus Cost

26. Earnings per share is equal to:
A. net income divided by the total number of shares outstanding.
B. net income divided by the par value of the common stock.
C. gross income multiplied by the par value of the common stock.
D. operating income divided by the par value of the common stock.
E. net income divided by total shareholders' equity.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-04 Value versus Cost

27. Dividends per share is equal to dividends paid:
A. divided by the par value of common stock.
B. divided by the total number of shares outstanding.
C. divided by total shareholders' equity.
D. multiplied by the par value of the common stock.
E. multiplied by the total number of shares outstanding.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-04 Value versus Cost

28. Calculate net income based on the following information.

Sales = $250.00
Cost of goods sold = $160.00
Depreciation = $35.00
Interest paid = $20.00
Tax rate = 34%
A. $23.10.
B. $11.90.
C. $35.00.
D. $46.20.
E. $36.30.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-04 Value versus Cost

29. The cash flow of the firm is defined as the cash flow of the assets. This cash flow must be equal to:
A. cash flow to equity minus cash flow to debtholders.
B. cash flow to debtholders minus cash flow to equity.
C. cash flow from changes in working capital plus cash flow to equity.
D. cash flow to equity plus cash flow to debtholders.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-04 Value versus Cost

30. When making financial decisions related to assets, you should:
A. always consider market values.
B. place more emphasis on book values than on market values.
C. rely primarily on the value of assets as shown on the balance sheet.
D. only consider market values if they are less than book values.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Easy
Topic: 02-04 Value versus Cost

31. From the following income statement information, calculate Johnson's after tax cash flow from operations.

Net sales = $2,500
Cost of goods sold = $1050
Operating expenses = $490
Depreciation = $300
Tax rate = 34%
A. $660.00
B. $990.00
C. $1257.00
D. $735.60
E. $1059.00

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-04 Value versus Cost

32. Over the year, the Rigem Co. had cash flow from operations of $938, and had net capital spending of $225. In addition, the firm's Net Working Capital increased by $73. What was Rigem's total cash flow?
A. $1,236.
B. $748.
C. $640.
D. $786.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-03 Debt versus Equity

33. The primary source of the firm's cash flow is usually:
A. net income.
B. tax credits.
<u>C.</u> earnings before interest and depreciation minus taxes.
D. capital spending after taxes.
E. working capital requirements.

Accessibility: Keyboard Navigation
Blooms: Remember
Difficulty: Easy
Topic: 02-04 Value versus Cost

34. Dorr Corp. had an ROA of 8%. Dorr's profit margin was 4% on sales of $250. What were total assets?
<u>A.</u> $125.
B. $500.
C. $30.
D. $220.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Hard
Topic: 02-02 Liquidity

35. Midget Co. has a profit margin on sales of 4% and a ROE of 18%. If Midget's debt-to-equity ratio is .8, what is the total asset turnover ratio?
<u>A.</u> 2.500.
B. 5.625.
C. 2.000.
D. 10.125.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Hard
Topic: 02-02 Liquidity

36. Donny Dell Inc. had a days in inventory of 5 (based on 365 days). The inventory turnover was:
A. 5.
B. 60.
C. 73.
D. cannot be figured without the inventory value.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Easy
Topic: 02-02 Liquidity

37. Donny Dell Inc. had a days in inventory (based on 365 days) of 5. Cost of goods sold were $4,526. Net working capital was $70 and total current assets were $400. What is Donny Dell's quick ratio?
A. 11.315.
B. 1.024.
C. 4.829.
D. 14.00.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Hard
Topic: 02-02 Liquidity

38. Donny Dell Inc.'s cost of goods sold were $4,526. They had net working capital of $70 and total current assets were $400. If inventory was 62 what is the current ratio of Donny Dell?
A. 7.3.
B. 5.71.
C. 1.21.
D. 4.71.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

39. Tan Co. had total operating revenues of $720 over the past year. During that time, average receivables were $90. What was the average collection period (ACP) given a 365-day year?
A. 8.00 days.
B. 4.56 days.
C. 40.97 days.
D. 45.63 days.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

40. Mirotronic Co. has a receivables turnover of 4 times. Sales are $20,000. What is the collection period? (Use 365 days in a year.)
A. 91.25 days
B. 90 days
C. 1.37 days
D. 21.92 days

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Easy
Topic: 02-02 Liquidity

41. The Cliplink Company has an equity multiplier of 3.36? What are the debt ratio and debt to equity ratios of Cliplink?
A. 0.70, 2.36.
B. 2.36, 0.70.
C. 0.30, 0.70.
D. cannot be calculated without values for debt or equity.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

42. The Hi-Lite Corp. had a profitable year and their ROE was 14.4%. The company paid out $1.20 of their earnings of $3.00 for the year. What is Hi-Lite's sustainable growth?
A. 17.20%
B. 8.64%
C. 5.76%
D. 43.20%

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

43. Sin Co. stock sells for $28.00 per share. The total market value of the equity is $40 million. The market-to-book ratio is 7. What is the book value per share?
A. $128.00.
B. $196.00.
C. $1.43.
D. $4.00.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

44. Assuming that the current ratio is currently 2, which of the following actions will increase it?
A. Purchasing inventory with cash.
B. Purchasing inventory on short-term credit.
C. Paying off a short-term bank loan with long-term debt.
D. A customer paying an overdue bill.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-02 Liquidity

45. Cos Co.'s after-tax net income was $120. Their interest paid was $50. Assuming the corporate tax is 40%, what is Cos CO.'s interest coverage ratio?
A. 6.7.
B. 2.4.
C. 1.44.
D. 5.0.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

46. The Hi-Lite Corp. had a profitable year and their ROE was 14.4%. The company paid out $1.20 of their earnings of $3.00 for the year. The market price of their stock at year end was $28. What was Hi-Lite's price-earnings ratio?
A. 23.33.
B. 9.33.
C. 4.03.
D. 12.10.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

47. Logit Co. paid dividends of $400. And retained 33.33% of their earnings. The sales for the year were $12,000 and total assets of 10,000. What was the rate of return on assets?
A. 5%.
B. 6%.
C. 10%.
D. 12%.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Hard
Topic: 02-02 Liquidity

48. The Lo-Gro Co. in 2014 had equity of $15 million, net income of $1,800,000 of which 60% was paid out as dividends. The sustainable growth rate for the Lo-Gro Co. is:
A. 0.48%.
B. 4.80%.
C. 0.72%.
D. 7.20%.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

49. The Lo-Gro Co. in 2014 had equity of $15 million, net income of $1,800,000 of which 60% was paid out as dividends. The ROE and retained earnings for the Lo-Gro Co. are:
A. 1.2%; $720,000.
B. 4.8%; $720,000.
C. 12%; $1,080,000.
D. 12%; $720,000.

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-02 Liquidity

50. Peggy Grey's Cookies has net income of $360. The firm pays out 40% of the net income to its shareholders as dividends. During the year, the company sold $80 worth of common stock. What is the cash flow to stockholders?
A. $64.
B. $136.
C. $144.
D. $224.

Cash flow to stockholders = .40($360) - $80 = $64

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-04 Value versus Cost

51. Pete's Boats has beginning long-term debt of $180 and ending long-term debt of $210. The beginning and ending total debt balances are $340 and $360, respectively. The interest paid is $20. What is the amount of the cash flow to creditors?

A. -$10.
B. $0.
C. $10.
D. $40.

Cash flow to creditors = $20 - ($210 - $180) = -$10

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-04 Value versus Cost

Short Answer Questions

52. Discuss the difference between book values and market values on the Statement of Financial Position and explain which is more important to the financial manager and why.

The accounts on the Statement of Financial Position are generally carried at historical cost, not market values. Although the book value of current assets and current liabilities may closely approximate market values, the same cannot be said for the rest of the Statement of Financial Position accounts. Ultimately, the financial manager should focus on the firm's stock price, which is a market value measure. Hence, market values are more meaningful than book values.

Accessibility: Keyboard Navigation
Blooms: Understand
Difficulty: Medium
Topic: 02-01 The Statement of Financial Position

53. The Simmons Company reported retained earnings in 2016 of $4750. In 2017, Simmons earned $1120 before taxes and paid a dividend of $730. Simmon's tax rate is 34%. What is Simmons' retained earnings?

$4750 + $1120(1 - .34) - $730 = $4759.20

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Easy
Topic: 02-01 The Statement of Financial Position

54. Pion Inc. reported current assets of $80 and fixed assets of $150 as of December 31. The company, as of December 31, also reports current liabilities of $72 and long-term liabilities of $149. Calculate Pion's shareholder's equity.

($80 + $150) - ($72 + $149) = $9

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-01 The Statement of Financial Position

55. Grady's Candies paid a total of $32 million in dividends in 2017. In addition, the company issued $22.5 million in new stock in that year. What was Grady's cash flow to stockholder's in 2017?

$32 - ($22.5) = ($9.5)

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Easy
Topic: 02-04 Value versus Cost

56. Based on the following information, calculate stockholders equity:

cash = $5.00
accounts payable = $12.00
other current liabilities = $65.00
accounts receivable = $20.00
inventory = $50.00
net fixed assets = $175.00
long-term debt = $40.00

($5 + $20 + $50 + $175) - ($12 + $65 + $40) = $133

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-01 The Statement of Financial Position

57. The Paymore Co. reported the following long-term liabilities and stockholder's equity for 2017:

Long-term debt	$200
Preferred stock	$80
Common stock	$30
Retained earnings	$375

In 2017, Paymore earned $125 in net income and paid a $40 dividend. What is the 2017 total common shareholder equity figure?

$30 + $375 + $125 - $40 = $490

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-01 The Statement of Financial Position

58.

Qwerty, Inc 2017 Income Statement ($ in millions)	
Net sales	$9,610
Less: cost of goods sold	6,310
Less: Depreciation	1,370
Earnings before interest and taxes	1,930
Less: Interest paid	630
Taxable Income	$1,300
Less: Taxes	455
Net income	$845

Qwerty, Inc Statement of Financial Position ($ in millions)					
	2016	**2017**		**2016**	**2017**
Cash	$310	$405	Accounts payable	$2,720	$2,570
Accounts rec.	2,640	3,055	Notes payable	100	0
Inventory	3,275	3,850	Total	$2,820	$2,570
Total	$6,225	$7,310	Long-term debt	7,875	8,100
Net fixed assets	10,960	10,670	Common stock	5,000	5,250
			Retained earnings	1,490	2,060
Total assets	$17,185	$17,980	Total liab. & equity	$17,185	$17,980

What is the change in the net working capital from 2016 to 2017?

($7,310 - $2,570) - ($6,225 - $2,820) = $1,335

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Medium
Topic: 02-03 Debt versus Equity

59.

Qwerty, Inc **2017 Income Statement** **($ in millions)**	
Net sales	$9,610
Less: cost of goods sold	6,310
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Qwerty, Inc Statement of Financial Position ($ in millions)					
	2016	**2017**		**2016**	**2017**
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Total	$6,225	$7,310	Long-term debt	7,875	8,100
Net fixed assets	10,960	10,670	Common stock	5,000	5,250
			Retained earnings	1,490	2,060
Total assets	$17,185	$17,980	Total liab. & equity	$17,185	$17,980

What is the cash flow of the firm for 2017?

Change in net working capital = ($75 + $502 + $640 - $405) - ($70 + $563 + $662 - $390) = -$93
Net capital spending = $1,413 - $1,680 + $210 = -$57
Earnings before interest and taxes = $785 - $460 - $210 = $115
Taxable income = $115 - $35 = $80
Taxes = .35($80) = $28
Operating cash flow = $115 + $210 - $28 = $297
Cash flow of the firm = $297 - (-$93) - (-$57) = $447

Accessibility: Keyboard Navigation
Blooms: Analyze
Difficulty: Hard
Topic: 02-04 Value versus Cost