Chapter 1 – The scope of corporate finance

MULTIPLE CHOICE

1. When identifying projects that increase company value, one of the tasks for financial managers is to identify those projects where:
   a. benefits are likely to exceed the project's costs
   b. taking the project will increase the book value of the company's common share
   c. taking the project will decrease the book value of the company's debt outstanding
   d. the project's cost are worthwhile for investors

   ANS: A PTS: 1 DIF: E
   REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking
   LOC: create a finance application in a computer spreadsheet and as an analyst using public information

2. Which finance career classification involves analysing a company's business processes and strategies as well as recommending a change in practice in order to make a company more competitive?
   a. Corporate finance
   b. Commercial banking
   c. Investment banking
   d. Consulting

   ANS: D PTS: 1 DIF: M
   REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking
   LOC: understand the role of the finance function in the enterprise

3. If you would like to trade debt and equity securities for customers, which finance career classification should you target?
   a. Corporate finance
   b. Commercial banking
   c. Investment banking
   d. Money management

   ANS: C PTS: 1 DIF: M
   REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking
   LOC: understand the role of the finance function in the enterprise

4. Which form of invested capital is subject to most of a company's business and financial risk?
   a. Debt capital
   b. Equity capital
   c. Borrowed capital
   d. Intellectual capital

   ANS: B PTS: 1 DIF: E
   REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
   LOC: understand shares and bonds

5. Which of the following is *not* a true capital-raising event for a company?
   a. Primary market transaction
   b. Secondary market transaction

c. Initial public offering
d. A corporate loan from a bank

ANS: B PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

6. Which of the following is *not* one of the five basic corporate finance functions?
a. External financing function
b. Capital budgeting function
c. Risk management
d. Auditing

ANS: D PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

7. Which of the following defines corporate finance?
a. The activities involved in managing cash (money) that flows through the business
b. The process of producing statements that disclose an organisation's financial status to management, investors and the government
c. The provision of financial data and advice to a company for use in the organisation and development of its business
d. The function that coordinates the efforts of people to accomplish goals and objectives by using available resources efficiently

ANS: A
REF: 1.2 Corporate Finance Essentials

8. What is the key responsibility of the financial management function?
a. To ensure that the company has enough funds on hand to support day-to-day operations
b. To support competitive decision making that helps management to plan, control and evaluate business processes
c. To provide independent assurance that an organisation's risk management, governance and internal control processes are operating effectively
d. To address accounting and treasury functions and to handle risk-related planning activities

ANS: A
REF: 1.2 Corporate Finance Essentials

9. What is the objective of the capital budgeting function?
a. To select the best projects in which to invest the company's funds based on expected risk and return
b. To provide useful information for financial decision making
c. To provide the necessary information to managers and supervisors to help them to discharge their functions of organising, planning, control and decision making
d. To measure performance, assess risk and to allocate scarce resources

ANS: A
REF: 1.2 Corporate Finance Essentials

10. What are the key objectives of the risk management function?
a. To identify, measure and manage the company's exposure to all types of risk

b. To maintain an optimal risk-return trade-off
c. To maximise share value
d. All of the above

ANS: A
REF: 1.2 Corporate Finance Essentials

11. The risk management function involves identifying, measuring and managing the company's exposure to all types of risk. Which of the following describes risks that businesses commonly face?
a. Losses that can result from adverse interest rate movements
b. Changes in commodity prices and fluctuations in currency values
c. Hardware or network connection failure and/or the death or injury of an employee
d. Options A and B are both correct.

ANS: A
REF: 1.2 Corporate Finance Essentials

12. By which two methods could risk be managed through the risk management function?
a. Risk shifting, and risk spreading (diversification)
b. Planning, and risk control
c. Risk avoidance, and risk mitigation
d. Risk prediction, and risk acceptance

ANS: A
REF: 1.2 Corporate Finance Essentials

13. Shifting the risk of your organisation is an example of:
a. corporate governance
b. risk management
c. financial management
d. external financing

ANS: B
REF: 1.2 Corporate Finance Essentials

14. Which of the following statements best describes diversification?
a. Diversification involves combining activities that give rise to risks in such a way that the overall risk of the combination is less than the risk of each item in the combination.
b. Diversification involves one organisation paying another entity to take on risk and to compensate the organisation in case of a negative outcome.
c. Diversification involves identifying, measuring and managing the company's exposure to all types of risk in order to maintain an optimal risk–return trade-off.
d. Diversification involves selecting the best projects in which to invest the company's funds.

ANS: A
REF: 1.2 Corporate Finance Essentials

15. William and Theodore have decided to start a travel business called Excellent Adventures. Because their business primarily involves time-travel, their clients may be harmed during a small but significant portion of the travels. Consequently, William and Theodore would like a business form that will shield their personal wealth from any legal claims that the company might be subject to after a travel mishaps. If William and Theodore are the only investors in this Australian domiciled company, which legal form of organisation would be best for Excellent Adventures to protect both William and Theodore?
    a. sole proprietorship
    b. partnership
    c. limited partnership
    d. corporation

    ANS: D
    A sole proprietorship is not possible with two owners.
    A partnership has joint and several liability, which will not help the owners.
    In a limited partnership, one partner must be the general partner, so this type of entity could not protect both owners.
    A corporation has limited liability.

    PTS: 1 DIF: H
    REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
    LOC: understand the role of the finance function in the enterprise

16. Which of the following is the main responsibility of the Australian Securities and Investments Commission (ASIC)?
    a. To be the corporate, markets and financial services regulator
    b. To formulate accounting standards according to corporation's act
    c. To oversee the effectiveness of financial reporting framework in Australia
    d. To advise political parties on their economic policy

    ANS: A
    REF: 1.2 Corporate Finance Essentials

17. Which of the following indicates the two basic sources of equity capital?
    a. Ordinary shares and preference shares
    b. Ordinary shares and convertible securities
    c. Convertible securities and notes receivable
    d. Convertible securities and preference shares

    ANS: A
    REF: 1.2 Corporate Finance Essentials

18. Which of the following is an example of a financial intermediary institution?
    a. Insurance companies
    b. Credit unions
    c. Mutual funds
    d. All of the above

    ANS: D
    REF: 1.2 Corporate Finance Essentials

19. Which of the following organisations is disadvantaged by unlimited personal liability?

a. Sole proprietorship
b. Partnership
c. Propriety limited company
d. Options A and B are both correct.

20. Within a limited partnership context, what are the conditions on a limited partner?
    a. There is a limit to the amount of capital that a limited partner can contribute, as mandated by law.
    b. There is a limit to the number of limited partners that the company may take on as investors.
    c. The limited partner must remain a low level employee and cannot ever serve in a managerial role in the company.
    d. A limited partner may not take any active role in the operation of the business.

ANS: D PTS: 1 DIF: H
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

21. The rules dictating voting procedures and other aspects of corporate governance for a corporation are:
    a. the minutes of the board of directors meeting
    b. the corporate charter
    c. the Institute for Corporate Governance (ICG) corporate governance procedures
    d. the Australian Securities and Investments Commission (ASIC) rules for corporate governance

ANS: B PTS: 1 DIF: M
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: understand shares and bonds

22. The ultimate owner(s) of an ongoing corporation are:
    a. the Federal Government
    b. the debt holders
    c. the equity holders
    d. the executive staff of the corporation

ANS: C PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: understand shares and bonds

23. Agency costs refer to:
    a. the costs associated with managing the demands of federal agencies
    b. the costs involved when converting an entity from a proprietorship to a corporation
    c. the costs that arise due to conflicts of interest between shareholders and managers
    d. the costs associated with managing customers

ANS: C PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: understand shares and bonds

24. Which of the following is a valid criticism concerning the goal of companies to maximise profits?
    a. Profit maximisation ignores expenses.
    b. Profit maximisation is completely unrelated to shareholder wealth.
    c. Profit maximisation may ignore the timing of those profits.

d. There are no valid criticisms of profit maximising companies.

ANS: C PTS: 1 DIF: M
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

25. Which of the following parties has the proper incentives to make risky, value-increasing investments for a company?
   a. Suppliers
   b. Creditors
   c. Shareholders
   d. Managers who are compensated only by salary

ANS: C PTS: 1 DIF: M
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand shares and bonds

26. An agent of a company could be:
   a. a 100 per cent owner of the company
   b. the agent in charge of auditing the company's tax return
   c. an employee who does not own any proportion of the company
   d. a supplier to the company

ANS: C PTS: 1 DIF: H
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand shares and bonds

27. Which of the following is *not* a way in which shareholders can attempt to overcome agency problems?
   a. Incurring costs to monitor managers
   b. Paying managers a good salary
   c. Relying on market forces to exert managerial discipline
   d. Paying the manager a proportion of the profits that the company generates

ANS: B PTS: 1 DIF: H
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand shares and bonds

28. Which of the following is the best bonding expenditure to help limit agency costs?
   a. auditing the managers work on a monthly basis
   b. entering a contract that forces the manager will forfeit a portion of his deferred compensation in the event of poor performance
   c. granting the manager a large number of options that will become valuable if the company performs well
   d. paying the manager a bonus if the company performs well

ANS: B PTS: 1 DIF: H
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

29. A root cause of company agency costs is:
   a. managerial carelessness
   b. a manager owning too much of the company's share

c. a manager's concern for his or her personal well-being
d. government agency filing requirements

ANS: C PTS: 1 DIF: H
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

30. Which of the following is a weakness of a sole proprietorship?
a. Unlimited life
b. Easy to form
c. Limited liability
d. Limited access to capital

ANS: D PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

31. Which of the following is a strength of a sole proprietorship?
a. Unlimited life
b. Easy to form
c. Limited liability
d. Limited access to capital

ANS: B PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

32. Which of the following is a strength of the corporate form of business?
a. Limited life of the business
b. Unlimited access to capital
c. Unlimited liability
d. Double taxation of income

ANS: B PTS: 1 DIF: M
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

33. Which of the following is *not* a strength of the corporate form of business?
a. Unlimited life of the business
b. Unlimited access to capital
c. Unlimited liability
d. Individual contracting

ANS: C PTS: 1 DIF: M
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

34. Shareholders are said to have a residual claim on a company's assets. What does this mean?
a. Shareholders have limited liability in their investment.
b. Shareholders do not receive any payoff from the company until all creditors are paid.
c. Shareholders are allowed to recover their investment first if the company experiences financial distress.
d. Shareholders have priority in electing the board of directors for the company.

ANS: B PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

35. Which market transactions generate new cash flow for the company?
    a. Primary market transactions
    b. Secondary market transactions
    c. Commodities market transactions
    d. Initial public offering (IPO) transactions

ANS: A PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

36. Which type of finance position focuses on preparing company financial plans and the evaluation of the company's financial ratios?
    a. Financial analyst
    b. Capital budgeting analyst
    c. Cash manager
    d. Portfolio manager

ANS: A PTS: 1 DIF: M
REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

37. Which of the following is *false* regarding debt capital?
    a. Debt holders receive interest payments at fixed intervals.
    b. Debt holders receive the amount of their loan (principal) at the debt's maturity date.
    c. Debt holders can force the company into bankruptcy if interest payments are not made.
    d. Debt holders have voting rights for the company's board of directors.

ANS: D PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand shares and bonds

38. Which of the following is *false* regarding equity capital?
    a. Common shareholders bear most of the company's business and financial risk.
    b. Preferred shareholders receive a fixed annual payment on their invested capital.
    c. Common shareholders have ownership in the company by voting for the company's management.
    d. Preferred shareholders can force the company into bankruptcy if dividend payments are not paid.

ANS: D PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand shares and bonds

39. What is a fiduciary?
    a. Someone who performs ratio analysis for a corporation
    b. Someone who invest and manages money on someone else's behalf
    c. Someone who manages the release of an initial public offering
    d. Someone who evaluates the performance of individual bonds

ANS: B PTS: 1 DIF: E
REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

40. What is the proper goal for a company's management?
    a. To maximise shareholder wealth
    b. To maximise net income or earnings
    c. To maximise sales revenue
    d. To minimise expenses

ANS: A PTS: 1 DIF: E
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

41. Which of the following is a basic guideline for financial decision making?
    a. Make decisions where the benefits exceed the costs.
    b. Make decisions where the total benefits exceed the total costs.
    c. Make decisions where the average benefits exceed the fixed costs.
    d. Make decisions where the average benefits exceed the average costs.

ANS: A PTS: 1 DIF: E
REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

42. Which of the following describes the collective action problem?
    a. When a CEO fails to represent the interest of shareholders in daily decisions of the company
    b. When the shareholders of a company fail to act in their own best interests
    c. When the managers of a company lack incentive to maximise shareholder wealth
    d. When an individual shareholder spends time and resources monitoring managers – and bearing the cost of this – while the benefits go to all the shareholders in the company

ANS: D PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

43. To maximise the value of a business, a company needs access to capital and to minimise risk for investors. Given these guidelines, which business form should maximise value for a company?
    a. sole proprietorship
    b. limited partnership
    c. general partnership
    d. corporation

ANS: D PTS: 1 DIF: H
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: understand shares and bonds

44. Which term refers to when a company offers shares to the general public for the first time?
    a. Initial public offering
    b. Initial placed offering
    c. Investment plan offer
    d. Investment of public offers

ANS: A PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

45. Which statement best describes the capital structure decision-making process for a company?
    a. The company finds the least expensive debt to finance its projects.
    b. The company finds a mixture of debt and equity to maximise company value.
    c. The company purchases a mixture of debt and equity to match the guidelines of the company charter.
    d. The company makes the necessary filings for an initial public offering (IPO).

ANS: B PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of capital budgeting and the cost of capital

46. Which of the following is *not* a duty of a financial manager?
    a. Budgeting
    b. Financial forecasting
    c. Product research
    d. Investment analysis

ANS: C PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

47. A business with a single owner is called a:
    a. partnership
    b. sole proprietorship
    c. corporation
    d. limited liability company (LLC)

ANS: B PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

48. Which of the following is *not* a possible career outcome of studying corporate finance?
    a. Financial analyst
    b. Mortgage banker
    c. Cash manager
    d. Controller

ANS: B PTS: 1 DIF: E
REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

49. Which of the following roles does *not* represent a career opportunity in money management?
    a. Portfolio manager
    b. Securities analyst
    c. Financial planner
    d. Capital budgeting analyst

ANS: D PTS: 1 DIF: E
REF: 1.1 The Role of Corporate Finance in Business NAT: Reflective thinking

LOC: understand the role of the finance function in the enterprise

50. Which of the following is considered a primary market transaction?
    a. Corporations sell securities to investors in exchange for cash.
    b. Investor A buys share from investor B.
    c. A company declares a dividend.
    d. A company makes a bank deposit.

ANS: A PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

51. Capital budgeting is the single most important activity of a company's financial manager. Which of the following is *not* a part of the capital budgeting process?
    a. Identifying potential investments
    b. Identifying investments that create shareholder value
    c. Developing new products
    d. Implementing and monitoring the selected investments

ANS: C PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of capital budgeting and the cost of capital

52. Which of the following describes the key objective of the corporate governance function?
    a. Deals with developing company-wide structures that force managers to act ethically and to make decisions that further the interests of the company's shareholders
    b. Deals with when one organisation pays another entity to take on the risk and compensates the other organisation in case of a negative outcome
    c. Deals with identifying, measuring and managing the company's exposure to all types of risk in order to maintain an optimal risk–return trade-off
    d. Deals with identifying the best projects in which to invest the company's funds

ANS: A PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

53. Which of the following is *not* considered a weakness of the sole proprietorship?
    a. Limited life
    b. Unlimited personal liability
    c. Simplicity
    d. Limited access to capital

ANS: C PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

54. Which of the following does *not* apply to a partnership?
    a. Limited life
    b. Limited access to capital
    c. A single owner
    d. Unlimited personal liability

ANS: C PTS: 1 DIF: E

REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

55. Which of the following is the responsibility of the board of directors of a corporation?
    a. Hiring and firing managers
    b. Managing day-to-day operations
    c. Amending the company's corporate charter when necessary
    d. Hiring and firing entry-level employees

ANS: A PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

56. Which of the following is *not* true?
    a. Preferred shareholders receive a fixed dividend each year.
    b. Common shareholders vote to elect the members of the board of directors.
    c. Preferred shareholders have a more senior claim on the company's assets in the event of bankruptcy than common shareholders.
    d. Preferred shareholders are considered the company's ultimate owners.

ANS: D PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: understand shares and bonds

57. What is the goal of financial management?
    a. To maximise corporate profits
    b. To maximise shareholder wealth
    c. To minimise costs
    d. To maximise earnings

ANS: B PTS: 1 DIF: E
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

58. You have just been hired as the CEO of a company. Your primary objective should be:
    a. to maximise the company's earnings
    b. to maximise profits
    c. to maximise the company's price of common share
    d. to eliminate the company's competitors

ANS: C PTS: 1 DIF: M
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

59. What should be the objective of focusing on stakeholders?
    a. Maximising shareholders' interests
    b. Picking shareholders' interests over shareholders' interests during conflicts
    c. Preserving shareholders' interests
    d. Disregarding shareholders' interests all together

ANS: C PTS: 1 DIF: M
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

60. In which form of business organisation is an agency problem most likely to occur?
    a. Sole proprietorship
    b. Corporation
    c. Partnership
    d. Limited liability company

ANS: B PTS: 1 DIF: M
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

61. Which of the following scenarios could be considered an example of an agency problem?
    a. Management decides to close a plant to lower operating costs.
    b. Management decides to go ahead with an expansion that is expected to benefit the company's value.
    c. The board of directors rewards management for the company's previous-year performance.
    d. Management decides to purchase a corporate jet.

ANS: D PTS: 1 DIF: M
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

62. Why do shareholders bear most of the risk of running a company?
    a. They only have a residual claim on the company's cash flows.
    b. They receive a salary from the company.
    c. They are guaranteed a fixed payout each quarter.
    d. Shares can be taken away at any time without notice.

ANS: A PTS: 1 DIF: E
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand shares and bonds

63. What do we call a possible conflict of interest between shareholders and management?
    a. Agency problem
    b. Stakeholder problem
    c. Double taxation
    d. Shareholders' dilemma

ANS: A PTS: 1 DIF: E
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

64. Which of the following is true?
    a. If a company files for bankruptcy, preferred shareholders' claims are paid prior to creditors' claims.
    b. If a company files for bankruptcy, preferred shareholders' claims are paid prior to common shareholders' claims.
    c. In the event of bankruptcy and subsequent liquidation, preferred shareholders only receive funds after creditors and common shareholders.
    d. If a company files for bankruptcy, preferred shareholders' claims are paid prior to managers' claims.

ANS: B PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand shares and bonds

65. A financial intermediary is an institution that:
a. lends money to borrowers and raises that capital by issuing equity
b. lends money to borrowers and raises that capital by issuing liabilities against itself
c. issues shares and sells shares in itself to generate cash for investing for the shareholders
d. issues shares and buys shares in itself to generate cash for investing for the shareholders

ANS: B PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

66. Venture capitalists:
a. are banks that provide capital only for low-risk corporations
b. will only make investments if there is no risk involved
c. are professional investors who provide capital to high-risk–high-return, rapidly-growing entrepreneurial businesses
d. are banks that provide capital exclusively to high-risk corporations

ANS: C PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

67. Working capital management:
a. involves managing the company's long-term assets, such as plant and equipment
b. requires very little in terms of people skills as it mostly involves analysing numbers
c. deals with the company's seasonal financing, inventory needs, collecting accounts receivable and investing surplus cash
d. involves managing long-term liabilities

ANS: C PTS: 1 DIF: M
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial analysis and cash flows

68. Diversifying among different suppliers is an example of:
a. capital budgeting
b. financial management
c. external financing
d. risk management

ANS: D PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire an understanding of risk and return

69. A share purchased on the Australian Securities Exchange (ASX) is an example of:
a. a primary money market transaction
b. a secondary money market transaction
c. a primary capital market transaction
d. a secondary capital market transaction

ANS: D PTS: 1 DIF: E

REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: acquire knowledge of financial markets and interest rates

70. When a corporation offers shares to the public for the first time, this is called a(n):
 a. IPO
 b. PPO
 c. NPO
 d. LBO

ANS: A PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

71. Hedging is:
 a. buying derivatives to take advantage of likely changes in the market
 b. buying a company's own share
 c. insuring against risks a company likely faces
 d. making sure that the hedges at company headquarters are well-pruned

ANS: C PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

72. Which agency oversees the fair reporting of financial information to investors of publicly traded shares?
 a. Australia Securities and Investments Commission (ASIC)
 b. Australian Taxation Office (ATO)
 c. Australian Prudential Regulation Authority (APRA)
 d. Australian Competition and Consumer Commission (ACCC)

ANS: A PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

73. Would it be reasonable for a successful manufacturing company that started as a sole proprietorship or a partnership to eventually adopt the corporate organisational form?
 a. No; the tax burden (double taxation) is too costly.
 b. No; the reporting burdens are too costly.
 c. No; once started as a sole proprietorship or partnership, companies are not allowed to change their form.
 d. Yes; the competitive disadvantages to sole proprietorship or partnership are too burdensome.

ANS: D PTS: 1 DIF: M
REF: 1.3 Legal Forms of Business Organisation NAT: Reflective thinking
LOC: assess the costs and benefits of business forms

74. Which of the following is *not* a stakeholder?
 a. Competitors
 b. Tax collection agencies
 c. Suppliers
 d. Customers

ANS: A PTS: 1 DIF: E
REF: 1.4 The Corporate Financial Manager's Goals NAT: Reflective thinking
LOC: understand the role of the finance function in the enterprise

SHORT ANSWER

1. List five basic functions that a financial manager performs.

ANS: Financing, financial management, capital budgeting, risk management and corporate governance
PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials

2. List three drawbacks of a partnership organisation.

ANS: Limited life, limited access to capital and unlimited personal liability
PTS: 1 DIF: E
REF: 1.3 Legal Forms of Business Organisation

3. What is the goal of the company's managers?

ANS: To maximise shareholder wealth
PTS: 1 DIF: E
REF: 1.4 The Corporate Financial Manager's Goals

4. Describe how agency cost be controlled in a company.

ANS: By providing compensation plans to control agency cost (e.g. executive compensation plans and share options)
PTS: 1 DIF: E
REF: 1.4 The Corporate Financial Manager's Goals

5. Explain how companies raise capital to fund their operation.

ANS: Companies have access to two broad types of capital: debt and equity.
PTS: 1 DIF: E
REF: 1.2 Corporate Finance Essentials