Financial Management 14th edition Titman Test Bank

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Financial Management: Principles & Applications, 14e **(Titman)**
Chapter 1 Getting Started-Principles of Finance

1) Which of the following statements best represents what finance is about?
A) How political, social, and economic forces affect corporations
B) Maximizing profits
C) The study of how people and businesses make investment decisions and how to finance those decisions.
D) Reducing risk
Answer: C
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

2) From a financial point of view, a company that decides to develop new product is making
A) a financing decision.
B) an investment decision.
C) a capital structure decision.
D) a cash flow decision.
Answer: B
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

3) Working capital management refers to
A) long-term financing decisions.
B) the management of cash flows.
C) investing in product development.
D) capital structure.
Answer: B
Diff: 2
AACSB: 5. Application of knowledge
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: capital structure
Principles: Principle 3: Cash Flows are the Source of Value

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4) Finance managers need to interact constantly with
A) marketing managers.
B) accounting staff.
C) management information systems staff.
D) all of the above.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

5) The personal decision to take a year off from work to obtain a graduate degree in business is primarily a(n)_____ decision.
A) social
B) financial
C) ethical
D) investment
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Revised
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

6) The area of finance that deals with long-term investment decisions is known as
A) capital structure.
B) working capital management.
C) financial strategy.
D) capital budgeting.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

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7) Capital structure refers to the financing of long-term investments.
Answer: TRUE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

8) Financial decisions can be difficult because the cost of investments can be estimated with greater confidence than future payoffs.
Answer: TRUE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

9) What are the three basic questions addressed by the study of investments?
Answer: 1. What long-term investments should the firm undertake?
2. How should the firm raise money to fund these investments?
3. How can the firm best manage its cash flows as they arise in its day to day operations?
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.1 Understand the importance of finance in your personal and professional lives and identify the three primary business decisions that financial managers make.
Keywords: what is finance?
Principles: Principle 3: Cash Flows are the Source of Value

10) Which of the following is NOT an advantage of the sole proprietorship?
A) Limited liability
B) No time limit imposed on its existence
C) No legal requirements for starting the business
D) None of the above
Answer: A
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: proprietorships
Principles: Principle 2: There Is a Risk-Return Tradeoff

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11) What is the chief disadvantage of the sole proprietorship as a form of business organization when compared to the corporate form?
A) Sole proprietorships are subject to double taxation of profits.
B) The cost of formation
C) Inadequate profit sharing
D) Owners have unlimited liability.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: proprietorships
Principles: Principle 2: There Is a Risk-Return Tradeoff

12) Which of the following is NOT true for limited partnerships?
A) Only limited partners can manage the business.
B) One general partner must exist who has unlimited liability.
C) Only the name of general partners can appear in the name of the firm.
D) Limited partners may sell their interest in the company.
Answer: A
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

13) The true owners of the corporation are the
A) holders of debt issues of the firm.
B) preferred stockholders.
C) board of directors of the firm.
D) common stockholders.
Answer: D
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

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14) In terms of organizational costs, which of the following sequences is generally correct, moving from lowest to highest cost?
A) General partnership, sole proprietorship, limited partnership, corporation
B) Sole proprietorship, general partnership, limited partnership, corporation
C) Corporation, limited partnership, general partnership, sole proprietorship
D) Sole proprietorship, general partnership, corporation, limited partnership
Answer: B
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

15) Assume that you are starting a business. Further assume that the business is expected to grow very quickly and a great deal of capital will be needed soon. What type of business organization would you choose?
A) Corporation
B) General Partnership
C) Limited liability company
D) Limited partnership
Answer: A
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

16) Which one of the following categories of owners enjoys limited liability?
A) General partners in a limited partnership or limited liability company.
B) Shareholders (common stock) of a corporation
C) Sole proprietors
D) Both A and B
Answer: B
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

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17) Which of the following is a characteristic of a limited partnership?
A) It allows one or more partners to have limited liability.
B) It requires one or more of the partners to be a general partner to whom the privilege of limited liability does not apply.
C) It prohibits the limited partners from participating in the management of the partnership.
D) All of the above.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

18) Limited liability companies (LLCs) differ from limited partnerships in that
A) owners of the LLC are subject to double taxation.
B) owners of the LLC have unlimited liability for the firm's debt.
C) owners of the LLC are not liable for the firm's debt.
D) owners of the LLC may not exceed 12 in number.
Answer: C
Diff: 2
AACSB: 4. Reflective thinking
Question Status: New question
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

19) Which of the following types of business forms is least risky to investors?
A) Sole proprietorship
B) Limited partnership
C) General partnership
D) A public corporation
Answer: D
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

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20) Which forms of organization are free of initial legal requirements?
A) Sole proprietorship
B) General partnership
C) Corporation
D) Both A and B
Answer: D
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

21) For these types of organization, no distinction is made between business and personal assets.
A) Sole proprietorship
B) General partnership
C) Limited partnership
D) Both A and B
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

22) Which of the following is a significant disadvantage of a general partnership?
A) The cost of forming it is high.
B) Each partner is fully responsible for the liabilities incurred by the partnership.
C) There is a risk associated with the industry in which it operates.
D) Forming the business is very complex.
Answer: B
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

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23) Which of the following forms of business organization is the dominant economic force in the United States?
A) The sole proprietorship
B) The general partnership
C) The limited partnership
D) The joint venture
E) The corporation
Answer: E
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

24) A limited partner is liable
A) for only his or her own share of the partnership's debts.
B) for his or her own share of the partnership's debts and contingently liable for the other partners shares.
C) only up to the amount invested by that partner.
D) for none of the partnership's debts.
Answer: C
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

25) A corporation is owned by
A) shareholders and partners.
B) the shareholders who hold the company's stock.
C) the Board of Directors
D) its Chief Executive Officer.
Answer: B
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

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26) The major sources of financing for corporations are
A) partners contributions.
B) exchanges between shareholders.
C) interest and dividends
D) Debt and equity.
Answer: D
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

27) The term stockholder is equivalent to
A) general partner.
B) creditor.
C) shareholder.
D) stakeholder.
Answer: C
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

28) The sole proprietorship is the same as the individual for liability purposes.
Answer: TRUE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: proprietorships
Principles: Principle 2: There Is a Risk-Return Tradeoff

29) In a general partnership, all partners have unlimited liability for the actions of any one partner when that partner is conducting business for the firm.
Answer: TRUE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

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30) There is no legal distinction made between the assets of the business and the personal assets of the owners in the limited partnership.
Answer: FALSE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

31) The owners of a corporation are liable for the corporation's obligations up to the amount of their investment.
Answer: TRUE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

32) General partners have unrestricted transferability of ownership, while limited partners must have the consent of all partners to transfer their ownership.
Answer: FALSE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

33) Ultimate control in a corporation is vested in the board of directors.
Answer: FALSE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

34) Owners must register and pay yearly fees to their State of residence when establishing a sole proprietorship.
Answer: FALSE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: proprietorships
Principles: Principle 2: There Is a Risk-Return Tradeoff

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35) Limited partners may actively manage the business.
Answer: FALSE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

36) The life of a corporation is not dependent upon the status of the investors.
Answer: TRUE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

37) If a limited partner dies or leaves the business, the partnership is dissolved and a new partnership must be formed.
Answer: FALSE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

38) In a sole proprietorship, the owner is personally responsible without limitation for the liabilities incurred.
Answer: TRUE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: proprietorships
Principles: Principle 2: There Is a Risk-Return Tradeoff

39) In a limited partnership, at least one general partner must remain in the association; the privilege of limited liability still applies to this partner.
Answer: FALSE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: corporation
Principles: Principle 2: There Is a Risk-Return Tradeoff

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40) In a general partnership, each partner is liable for the partnership's obligations only up to a percentage of the obligation equal to that partner's percentage of ownership of the partnership.
Answer: FALSE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.2 Identify the key differences among the three major legal forms of business.
Keywords: partnerships
Principles: Principle 2: There Is a Risk-Return Tradeoff

41) Maximization of shareholder wealth as a goal is superior to accounting profit maximization because
A) it considers the time value of the money.
B) following the shareholder wealth maximization goal will ensure high stock prices.
C) accounting profits are not the same as cash flows.
D) A and C.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: geometric average return
Principles: Principle 3: Cash Flows are the Source of Value

42) Which of the following best describes the goal of the firm?
A) The maximization of the total market value of the firm's common stock
B) Profit maximization
C) Risk minimization
D) None of the above
Answer: A
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

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43) Profit maximization does not adequately describe the goal of the firm because
A) profit maximization does not require the consideration of risk.
B) profit maximization ignores the timing of a project's return.
C) maximization of dividend payout ratio is a better description of the goal of the firm.
D) A and B.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

44) Which of the following goals of the firm is equivalent to the maximization of shareholder wealth?
A) Profit maximization
B) Risk minimization
C) Maximization of the total market value of the firm's common stock
D) None of the above
Answer: C
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

45) If managers are making decisions to maximize shareholder wealth, then they are primarily concerned with making decisions that should
A) positively affect profits.
B) increase the market value of the firm's common stock.
C) either increase or have no effect on the value of the firm's common stock.
D) accomplish all of the above.
Answer: B
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

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46) Profit maximization is not an adequate goal of the firm when making financial decisions because
A) it does not necessarily reflect shareholder wealth maximization.
B) it ignores the risk inherent in different projects that will generate the profits.
C) it ignores the timing of a project's returns.
D) all of the above are correct.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

47) Which of the following goals is in the best long-term interest of stockholders?
A) Profit maximization
B) Risk minimization
C) Maximizing of the market value of the existing shareholders' common stock
D) Maximizing sales revenues
Answer: C
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

48) If managers do not pursue the goal of maximizing shareholder wealth
A) they concentrate on more important matters like growing market share.
B) they can focus more on social responsibilities.
C) they are likely to lose their jobs.
D) they can focus more on long-term profitability.
Answer: C
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 5: Individuals Respond to Incentives.

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49) What does the agency problem refer to?
A) The conflict that exists between the board of directors and the employees of the firm.
B) The problem associated with financial managers and Internal Revenue agents.
C) The conflict that exists between stockbrokers and investors.
D) The problem that results from potential conflicts of interest between the manager of a business and the stockholders.
Answer: D
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: agency
Principles: Principle 5: Individuals Respond to Incentives.

50) Managers of corporations need to act in an ethical manner
A) because ethics violations will be punished by the law.
B) because a business must be trusted by investors, customer and the public if it is to succeed.
C) because business managers must answer to a higher authority.
D) because ethical behavior is its own justification.
Answer: B
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: ethics
Principles: Principle 5: Individuals Respond to Incentives.

51) In regard to the agency problem, _____ are the principal owners of a corporation.
A) shareholders
B) managers
C) employees
D) suppliers
Answer: A
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: goal of the firm
Principles: Principle 5: Individuals Respond to Incentives.

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52) Serious ethical violations by corporations such as Enron led to the passage of
A) The Dodd-Frank Act.
B) the Insider Trading Act of 1988.
C) The Sarbanes-Oxley Act.
D) All of the above.
Answer: C
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 5: Individuals Respond to Incentives.

53) Most criticism of the Sarbanes-Oxley Act focuses on
A) the excessive cost of compliance.
B) inadequate penalties for violations.
C) diminished competitiveness of U.S. corporations in international markets.
D) decreased confidence in financial reporting.
Answer: A
Diff: 2
AACSB: 1. Ethical understanding and reasoning
Question Status: New question
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: corporation
Principles: Principle 5: Individuals Respond to Incentives.

54) The Sarbanes-Oxley was passed in
A) 1933 to separate commercial banking from investment banking.
B) 2002 after the ENRON bankruptcy exposed unethical behavior by the company's executives and accountants.
C) 2008 after the collapse of the subprime mortgage market.
D) 2010 to protect consumers from financial fraud.
Answer: B
Diff: 2
AACSB: 1. Ethical understanding and reasoning
Question Status: New question
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: corporation
Principles: Principle 5: Individuals Respond to Incentives.

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55) The Sarbanes-Oxley Act of 2002
A) protects managers of publicly held corporations from frivolous lawsuits for unethical behavior.
B) prohibits managers of publicly held corporations from personally profiting from non-public information.
C) holds those who influence corporate decisions legally accountable for unethical conduct.
D) allows corporate accountants greater latitude in the application of generally accepted accounting principles.
Answer: C
Diff: 2
AACSB: 1. Ethical understanding and reasoning
Question Status: New question
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: corporation
Principles: Principle 5: Individuals Respond to Incentives.

56) The goal of the firm should be the maximization of profit.
Answer: FALSE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

57) One of the problems associated with profit maximization is that it ignores the timing of a project's return.
Answer: TRUE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

58) The goal of profit maximization is equivalent to the goal of maximization of share value.
Answer: FALSE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

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59) The goal of profit maximization ignores the timing of profit.
Answer: TRUE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: goal of the firm
Principles: Principle 3: Cash Flows are the Source of Value

60) The goal of maximize shareholder wealth inevitably conflicts with socially responsible behavior on the part of corporation.
Answer: FALSE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: ethics
Principles: Principle 4: Market Prices Reflect Information

61) The Sarbane-Oxley Act addresses insider trading by members of Congress.
Answer: FALSE
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: ethics
Principles: Principle 5: Individuals Respond to Incentives.

62) A reputation for unethical behavior can negatively affect the value of a company's stock.
Answer: TRUE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: ethics
Principles: Principle 5: Individuals Respond to Incentives.

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63) The agency problem arises due to the separation of ownership and control in a corporation.
Answer: TRUE
Diff: 1
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: goal of the firm
Principles: Principle 5: Individuals Respond to Incentives.

64) Briefly discuss the incentives for financial managers to conduct their business in an ethical manner.
Answer: Extreme ethical lapses such as those evident in the Madoff Ponzi scheme may also break laws and result in fines or imprisonment. In less extreme cases, deceptive accounting practices or sales techniques once exposed lead to a loss of trust. Because individuals and firms are reluctant to do business with those they mistrust, a reputation for unethical behavior over the long run leads to adversarial relations with business partners, a loss of customers, and destruction of the firm's value.
Diff: 2
AACSB: 4. Reflective thinking
Question Status: Previous edition
Objective: 1.3 Understand the role of the financial manager within the firm and the goal for making financial choices.
Keywords: ethics
Principles: Principle 5: Individuals Respond to Incentives.

65) Consider the following equally likely project outcomes:

	Profit	
	X	Y
Pessimistic prediction	$ 0	$500
Expected outcome	$ 500	$500
Optimistic prediction	$1000	$500

A) Investors will prefer project X because it potentially offers a higher profit.
B) Investors will reject both projects because the profit is too low.
C) Investors will prefer project Y because the expected return is the same as for project X but the outcome is certain.
D) Since Projects X and Y have the same expected outcomes of $500, investors will view them as identical in value.
Answer: C
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

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66) Consider the timing of the profits of the following certain investment projects:

	Profit	
	L	S
Year 1	$ 0	$ 3000
Year 2	$ 3000	$ 0

A) Project S is preferred to Project L.
B) Project L is preferred to Project S.
C) Projects S and L are equally desirable.
D) A goal of profit maximization would favor Project S only.
Answer: A
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: time value of money
Principles: Principle 1: Money Has a Time Value

67) In finance, we assume that investors are generally
A) neutral to risk.
B) averse to risk.
C) fond of risk.
D) none of the above.
Answer: B
Diff: 1
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
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68) Consider cash flows for Projects X and Y such as:

	Project X	Project Y
Year 1	$3000	$ 0
Year 2	$ 0	$3000

A rational person would prefer receiving cash flows sooner because
A) the money can be reinvested.
B) the money is nice to have around.
C) the investor may be tired of a particular investment.
D) the investor is indifferent to either proposal.
Answer: A
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: time value of money
Principles: Principle 1: Money Has a Time Value

69) Which of the following should be considered when assessing the financial impact of business decisions?
A) The amount of projected earnings
B) The risk-return tradeoff
C) The timing of projected earnings; i.e., when they are expected to occur
D) All of the above
Answer: D
Diff: 1
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

70) Which of the following is most likely to motivate executives to maximize shareholder wealth?
A) Tying bonuses to cost reductions and meeting budget goals.
B) Offering them relatively high salaries.
C) Tying annual bonuses to increases in annual profits.
D) Compensating them with stock options that can only be exercised after five years.
Answer: D
Diff: 1
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: agency
Principles: Principle 5: Individuals Respond to Incentives.

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71) If one security has a greater risk than another security, how will investors respond?
A) They will require a lower rate of return for the investment that has greater risk.
B) They would be indifferent regarding their expectation of rates of return for either investment.
C) They will require a higher rate of return for the investment that has greater risk.
D) None of the above.
Answer: C
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

72) How could you compensate an investor for taking on a significant amount of risk?
A) Increase the expected rate of return
B) Raise more debt capital
C) Offer stock at a higher price
D) Increase sales
Answer: A
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

73) If an investor had a choice of receiving $1,000 today, or $1,000 in five years, which would the average investor prefer?
A) $1,000 in five years because they are not good at saving money.
B) $1,000 today because it will be worth more than $1,000 received in five years.
C) $1,000 in five years because it will be worth more than $1,000 received today.
D) Investors would be indifferent to when they would receive the $1,000.
E) None of the above.
Answer: B
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: time value of money
Principles: Principle 1: Money Has a Time Value

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74) Why do investors prefer receiving cash sooner rather than later, according to finance theory?
A) Incremental profits are greater than accounting profits.
B) Money received earlier can be reinvested and returns can be increased.
C) Tax considerations are important when investing.
D) Diversification leads to increased value.
Answer: B
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: time value of money
Principles: Principle 1: Money Has a Time Value

75) Investors choose to invest in higher risk investments because these investments offer higher
A) expected returns.
B) inflation.
C) actual returns.
D) future consumption.
Answer: A
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

76) Foregoing the earning potential of a dollar today is referred to as the
A) time value of money.
B) opportunity cost concept.
C) risk/return tradeoff.
D) creation of wealth.
Answer: B
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: opportunity cost
Principles: Principle 1: Money Has a Time Value

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77) In measuring value, the focus should be on
A) cash flow.
B) accounting profits.
C) time value of money.
D) earnings per share.
Answer: A
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: cash flow
Principles: Principle 3: Cash Flows are the Source of Value

78) Which of the following is a characteristic of an efficient market?
A) Small number of individuals
B) Opportunities exist for investors to profit from publicly available information.
C) Security prices reflect fair value of the firm.
D) Immediate response occurs for new public information.
Answer: C
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: efficient markets
Principles: Principle 4: Market Prices Reflect Information

79) Which of the following factors is most important in investment decisions?
A) The change in earnings before taxes.
B) The change in gross sales revenue.
C) The change in net income.
D) The change in after-tax cash flow.
Answer: D
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: cash flow
Principles: Principle 3: Cash Flows are the Source of Value

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80) Investors prefer $1 today versus $1 in the future due to
A) time value of money.
B) response to incentives.
C) the need for immediate gratification.
D) A and B.
Answer: A
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: time value of money
Principles: Principle 1: Money Has a Time Value

81) In 2016, shares of Chipotle Mexican Grill lost more than half their value after widely reported incidents of customers suffering from food poisoning after eating at their restaurants. The change in stock price illustrates which principle?
A) Market prices reflect information.
B) Individuals respond to incentives.
C) Cash flows are the source of value.
D) The time-value of money.
Answer: A
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: New question
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: efficient markets
Principles: Principle 4: Market Prices Reflect Information

82) For the risk-return principle implies that the more risky a given course of action, the higher the expected return must be.
Answer: TRUE
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

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83) The financial manager should examine available risk-return trade-offs and make his decision based upon the greatest expected return.
Answer: FALSE
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

84) Only a few financial decisions involve some sort of risk-return tradeoff.
Answer: FALSE
Diff: 1
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

85) In efficient markets, prices rapidly adjust to new information.
Answer: TRUE
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: New question
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: efficient markets
Principles: Principle 4: Market Prices Reflect Information

86) Rewarding executives for increasing quarterly earnings will motivate them to act in the long-term best interests of shareholders.
Answer: FALSE
Diff: 1
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: incentives
Principles: Principle 5: Individuals Respond to Incentives.

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87) In an efficient market, prices will quickly adjust to new information.
Answer: TRUE
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: efficient markets
Principles: Principle 4: Market Prices Reflect Information

88) Briefly discuss why financial decision makers must focus on incremental cash flows when evaluating new projects.
Answer: Incremental cash flows describe the total cash effect on the company, looking at the difference between total cash flow to the company with the cash flow, and without the cash flow. The company can then value these cash flows and see if the company is worth more with the project or without the project.
Diff: 3
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: incremental cash flows
Principles: Principle 3: Cash Flows are the Source of Value

89) Discuss the risk/return tradeoff and how it relates to finance.
Answer: As people are risk averse, they need a higher return as the risk gets higher. This means that investors will need a higher return on bonds that they do not consider to be as safe as other bonds, and they will need a higher return on stock when the company in question's stock seems to be riskier than the stock of other companies.
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: risk, return
Principles: Principle 2: There Is a Risk-Return Tradeoff

90) Why do you think many companies compensate executives with options based on long-term increases in the value of the company's stock?
Answer: Tying executive compensation to long-term increases in the stock price makes sense because they are supposed to be working to maximize shareholder wealth. Stock-based compensation plans imply that decisions made to benefit shareholders will also benefit themselves.
Diff: 2
AACSB: 3. Analytic thinking skills
Question Status: Previous edition
Objective: 1.4 Explain the five principles of finance that form the basis of financial management for both businesses and individuals.
Keywords: incentives
Principles: Principle 5: Individuals Respond to Incentives.

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