BUSINESS-ENVIRONMENT-AND-CONCEPTS Q&As

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QUESTION 1

Assume that each day a company writes and receives checks totaling $10,000. If it takes five days for the checks to clear and be deducted from the company\\'s account, and only four days for the deposits to clear, what is the float?

A. $10,000

B. $0

C. $(10,000)

D. $25,000

Correct Answer: A

Choice "a" is correct. $10,000. Float is the difference between the balance of checks outstanding, which have not cleared the bank and deposits made but which have not yet cleared the bank here.

$10,000/day checks drawn but not cleared	×	5 days	= $50,000
Less $10,000/day checks received but not cleared	×	4 days	= (40,000)
Positive "float"			= $10,000

Choices "b", "c", and "d" are incorrect, per the above calculation.

QUESTION 2

An increase in the money supply leads to:

A. A decline in interest rates, an increase in investment and an increase in aggregate demand.

B. A decline in interest rates, a decrease in investment and an increase in aggregate demand.

C. An increase in interest rates, a decrease in investment and a decrease in aggregate demand.

D. An increase in the money supply has no effect on interest rates or investment.

Correct Answer: A

Choice "a" is correct. Expansionary monetary policy results when the Fed increases the money supply.

Expansionary monetary policy affects the economy through the following chain of events: (1) an increase in the money supply causes interest rates to fall, (2) falling interest rates stimulate the desired levels of firm investment and household consumption, (3) increases in desired investment and consumption cause an increase in aggregate demand, and (4) aggregate demand shifts to the right causing real GDP and the price level to rise.

Choice "b" is incorrect. An increase in the money supply causes investment to increase, not decrease.

Choice "c" is incorrect. An increase in the money supply causes interest rates to decrease, not increase,

investment to increase, not decrease and aggregate demand to increase, not decrease.

Choice "d" is incorrect per above Explanation.

QUESTION 3

Which of the following statements is correct with respect to the differences and similarities between a corporation and a limited partnership?

A. Stockholders may be entitled to vote on corporate matters but limited partners are prohibited from voting on any partnership matters.

B. Stock of a corporation may be subject to the registration requirements of the federal securities laws but limited partnership interests are automatically exempt from those requirements.

C. Directors owe fiduciary duties to the corporation and limited partners owe such duties to the partnership.

D. A corporation and a limited partnership may be created only under a state statute and each must file a copy of its organizational document with the proper governmental body.

Correct Answer: D

Choice "d" is correct. Both a limited partnership and a corporation:

1.

Can only be created by statute, and

2.

Each must file a copy of its certificate with the proper state agency.

Choice "a" is incorrect. There are instances in which limited partners do vote on certain partnership matters

(e.g., approve new general or limited partners).

Choice "b" is incorrect. Limited partnership interests are not automatically exempt from the federal

securities laws.

Choice "c" is incorrect. Limited partners do not owe a fiduciary duty to the limited partnership.

QUESTION 4

Kemple Cleaning Services is a newly established janitorial firm, and the owner is deciding which type of checking account to open. Kemple is planning to keep a $500 minimum balance in the account for emergencies and plans to write an average of 80 checks per month. The bank charges $10 per month plus a $0.10 per check charge for a standard business checking account with no minimum balance. Kemple also has the option of a premium business checking account, which requires a $2,500 minimum balance but has no monthly fees or per check charges. If

Kemple\\'s cost of funds is 10 percent, which account should Kemple choose?

A. Standard account, since the savings is $34 per year.

B. Premium account, since the savings is $34 per year.

C. Standard account, since the savings is $16 per year.

D. Premium account, since the savings is $16 per year.

Correct Answer: D

Choice "d" is correct. The total cost for a standard account is:

Monthly charge		$ 10
Per check charge ($.10 × 80 checks)		8
Total per month		$ 18
Total per year standard ($18 × 12)	$216	

Cost per year for premium is cost of the extra amount ($2,000) that Kemple must maintain in the account.

Total per year premium (10% ?$2,000) = $200

The premium account will save $16.

Choices "a", "b", and "c" are incorrect, per the above calculation.

QUESTION 5

McLean Inc. is considering the purchase of a new machine that will cost $150,000. The machine has an estimated useful life of three years. Assume for simplicity that the equipment will be fully depreciated 30, 40, and 30 percent in each of the three years, respectively. The new machine will have a $10,000 resale value at the end of its estimated useful life. The machine is expected to save the company $85,000 per year in operating expenses. McLean uses a 40 percent estimated income tax rate and a 16 percent hurdle rate to evaluate capital projects. Discount rates for a 16 percent rate are as follows:

	Present Value of $1	Present Value of an Ordinary Annuity of $1
Year 1	.862	.862
Year 2	.743	1.605
Year 3	.641	2.246

The payback period for this investment would be:

A. 2.95 years

B. 1.76 years

C. 2.09 years

D. 2.94 years

Correct Answer: C

Choice "c" is correct. 2.09 years payback period.

	19X0	19X1	19X2	19X3	
Initial cash outflow	$(150,000)				
After tax cash inflows:					
Depreciation tax shield		$18,000	$24,000	$18,000	[Note A]
Annual savings		51,000	51,000	51,000	[Note B]
Salvage (realized at end of year)					Not Applicable
After tax cash flow	(150,000)	69,000	75,000	69,000	
	Ø	Ø			
Unrecovered cost	(150,000)	(81,000)	**(6,000)**		

Note A The tax shields are calculated as follows:

	Depr. Basis		Depr %		Tax Rate 63		
Year 1:	$150,000	x	.30	x	.40	=	**$18,000**
Year 2:	150,000	x	.40	x	.40	=	**24,000**
Year 3:	150,000	x	.30	x	.40	=	**18,000**

Note B The annual savings is calculated as follows:

Operating expenses saved	$85,000
Times: 1 - tax rate (1 - .40)	x .60
Annual savings	**$51,000**

At the beginning of year 3, $6,000 is needed to recover the investment. Because an inflow of $69,000 is expected throughout the year, only 6,000 ?69,000 = .09 years is needed to recover the $6,000. Thus, the payback is 2.09 years. The $6,000 in salvage is excluded from the totals for year 3. Amounts are not realized until the end of the year while savings and depreciation tax shield occur throughout the year and are relevant to the partial year payback.

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