# BUSINESS-ENVIRONMENT-AND-CONCEPTS Q&As

Certified Public Accountant (Business Environment & Concept)

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**QUESTION 1**

All of the following capital budgeting analysis techniques use cash flows as the primary basis for the calculation, except for the:

A. Net present value.

B. Internal rate of return.

C. Discounted payback period.

D. Accounting rate of return.

Correct Answer: D

Choice "d" is correct. The accounting rate of return does not use cash flows as the primary basis for the calculation. It measures the accrual accounting return instead of cash flows:

$$\text{Accounting rate of return} = \frac{\text{Increase in expected average annual net income}}{\text{Average investment}}$$

Choice "a" is incorrect. Net present value method discounts cash flows for an investment over its life to time period zero using a desired or minimum rate of return. Choice "b" is incorrect. Internal rate of return (IRR) determines the compound interest rate of an investment where the present value of the cash inflows equals the present value of the cash outflows. The IRR is the discount rate that results in a net present value of zero. Choice "c" is incorrect. The discounted payback period is the time period required for discounted cash inflows to equal the initial investment. The time value of money is considered.

**QUESTION 2**

The marketable securities with the least amount of default risk are:

A. Federal government agency securities.

B. U.S. treasury securities.

C. Repurchase agreements.

D. Bankers\\' acceptances.

Correct Answer: B

Choice "b" is correct. Default risk is the risk that the security will not be repaid because the issuing entity is insolvent or illiquid. U.S. Treasury securities are issued by the Treasury Department, which has virtually no risk of being insolvent or illiquid. Choice "a" is incorrect. Securities issued by certain federal government agencies carry slightly more default risk than U.S. treasuries because these agencies are (usually) not as large or liquid as the U.S. Treasury. Choice "c" is incorrect. Repurchase agreements are sales by dealers in government securities who agree to repurchase these securities at a specific time and price. The risk of default is high because it is based upon the ability of the dealer to repurchase the securities. Choice "d" is incorrect. Bankers\\' acceptances are drafts drawn on a bank, which guarantees payment at maturity. The default risk is higher because the execution of the acceptance is based upon the solvency of the bank.

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**QUESTION 3**

White, Grey, and Fox formed a limited partnership. White is the general partner and Grey and Fox are the limited partners. Each agreed to contribute $200,000. Grey and Fox each contributed $200,000 in cash while White contributed $150,000 in cash and $50,000 worth of services already rendered. After two years,

the partnership is insolvent. The fair market value of the assets of the partnership is $150,000 and the

liabilities total $275,000. The partners have made no withdrawals.

If Fox is insolvent and White and Grey each has a net worth in excess of $300,000, what is White\\'s

maximum potential liability in the event of a dissolution of the partnership?

A. $62,500

B. $112,500

C. $125,000

D. $175,000

Correct Answer: C

Rule: The liability of a limited partner for partnership debts is limited to the extent of the capital, which he has contributed or has agreed to contribute. A general partner, however, is liable for all partnership debts and liabilities. Choice "c" is correct. In this case, both Grey and Fox are limited partners and, thus, their respective maximum liability for partnership debts may not exceed their contributions ($200,000 each). Because White is a general partner, however, he will be personally liable for the excess of any debt remaining after assets have been applied upon a dissolution. Therefore, White will be liable for $125,000 (the difference between the fair market value of assets ($150,000) and partnership liabilities ($275,000) at dissolution). Choices "a", "b", and "d" are incorrect, per the above rule.

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**QUESTION 4**

Spotech Co.\\'s budgeted sales and budgeted cost of sales for the coming year are $212,000,000 and $132,500,000 respectively. Short-term interest rates are expected to average 5 percent. If Spotech could increase inventory turnover from its current 8 times per year to 10 times per year, its expected cost savings in the current year would be:

A. $165,625

B. $331,250

C. $81,812

D. $250,000

Correct Answer: A

Choice "a" is correct. $165,625 expected cost savings by increasing inventory turnover from its current 8 times to 10 times per year.

| Cost Of Sales | | Inventory Turnover | | Avg. Inventory | |
|---|---|---|---|---|---|
| $132,500,000 | ÷ | 8 | = | $16,562,500 | |
| 132,500,000 | ÷ | 10 | = | 13,250,000 | |
| | | | | 3,312,500 | Inventory Decrease |
| | | | | × 5% | Interest Rate |
| | | | | $ 165,625 | Cost Savings |

**QUESTION 5**

Under the Revised Model Business Corporation Act, when a corporation\\'s bylaws grant stockholders preemptive rights, which of the following rights is(are) included in that grant?

| | *The right to a proportionate share of corporate assets remaining on corporate dissolution* | *The right to purchase a proportionate share of newly issued stock* |
|---|---|---|
| **A.** | Yes | Yes |
| **B.** | Yes | No |
| **C.** | No | Yes |
| **D.** | No | No |

A. Option A

B. Option B

C. Option C

D. Option D

Correct Answer: C

Rule: Preemptive rights provide a shareholder with a right of first refusal to buy a share of newly issued

shares sufficient to maintain the shareholder\\'s proportionate share of rights in any newly issued shares.

Rule: Preemptive rights do not provide a shareholder with the right to a proportionate share of corporate

assets on dissolution.

Choice "c" is correct. "No - Yes."

Choices "a", "b", and "d" are incorrect, per the above rules.