## Question #1 of 12

Question ID: 1457986

Which of the following statements *most* accurately characterizes how debt ratings may affect a firm's capital structure policy?

**A)** A firm may be deterred from increasing the use of debt to avoid having its credit rating reduced below some minimum acceptable level.

**B)** Firms that have their credit ratings reduced below investment grade are not able to issue additional debt.

**C)** Because credit ratings are based upon cash flow coverage of interest expense, they are not influenced by the firm’s capital structure.

---

## Question #2 of 12

Question ID: 1457992

The conclusion of Modigliani and Miller's capital structure model with taxes is that:

**A)** capital structure decisions do not affect the value of a firm.

**B)** there is a trade-off between tax savings on debt increased risk of bankruptcy.

**C)** firms should be financed with all debt.

---

## Question #3 of 12

Question ID: 1463597

According to pecking order theory, which of the following lists *most* accurately orders financing preferences from most to least preferred?

**A)** Debt financing, retained earnings, and raising external equity.

**B)** Retained earnings, raising external equity, and debt financing.

**C)** Retained earnings, debt financing, and raising external equity.

---

## Question #4 of 12

Question ID: 1457993

Under the assumptions of Modigliani and Miller's Proposition I, the value of a firm:

**A)** decreases as the use of equity financing rises.

**B)** increases as the use of debt financing rises.

**C)** is not affected by its capital structure.

---

## Question #5 of 12

Question ID: 1457995

Which of the following is *least likely* to be a reason why a firm's actual capital structure may vary from the target capital structure?

**A)** The firm decides to issue additional equity because management believes the firm’s stock is overpriced.

**B)** The firm decides to issue additional debt due to a temporary discount in underwriting fees for corporate debt.

**C)** The firm decides to finance a low risk project with 100% debt to improve the project’s profitability.

---

## Question #6 of 12

Question ID: 1457994

Which of the following statements regarding Modigliani and Miller's Proposition II with taxes is *most accurate*?

**A)** Companies should use a 50% equity/50% debt capital structure to maximize value.

**B)** The value of the firm is maximized at the point where the WACC is minimized.

**C)** The tax shield provided by debt causes the WACC to increase as leverage increases.

---

## Question #7 of 12

Question ID: 1457991

Removing the assumption of no taxes, but keeping all of Modigliani and Miller's other assumptions, which of the following would be the optimal capital structure for maximizing the value of a firm?

**A)** 100% equity.

**B)** 50% debt and 50% equity.

**C)** 100% debt.

---

## Question #8 of 12

Question ID: 1457990

According to the static trade-off theory:

**A)** the amount of debt used by a company should decrease as the company's corporate tax rate increases.

**B)** there is an optimal proportion of debt that will maximize the value of the firm.

**C)** new debt financing is always preferable to new equity financing.

---

## Question #9 of 12

Question ID: 1463598

Which of the following statements *most* correctly characterizes the pecking order theory of capital structure?

**A)** Firms have a preference ordering for capital sources, preferring internally-generated equity first, new debt capital second, and externally-sourced equity as a last resort.

**B)** Firms will seek to use debt financing up to the point that the value of the tax shield benefit is outweighed by the costs of financial distress.

**C)** Regardless of how the firm is financed, the overall value of the firm and aggregate value of the claims issued to finance it remain the same.

---

## Question #10 of 12

Question ID: 1457988

A company will typically use debt for the largest percentage of its financing during its:

**A)** maturity stage.

**B)** start-up stage.

**C)** growth stage.

## Question #11 of 12

Question ID: 1457996

When interest rates have fallen to low levels that are expected to persist, firms are *most likely* to have a preference for:

**A)** issuing debt.

**B)** issuing equity.

**C)** repurchasing equity.

## Question #12 of 12

Question ID: 1457989

Companies moving from the start-up stage to the growth stage *most likely* exhibit increasing:

**A)** debt financing costs.

**B)** business risk.

**C)** cash flow.