Final Review

Chapter 13

1. A limited liability company (LLC) **limits financial exposure of its owners**.
2. Which of the following business organizations limit the liability of some or all of their owners to the extent of their investment in the company?
    - **corporations and limited partnerships**
3. Accounting practices and procedures used to prepare financial statements are called: **GAAP**
4. The U.S. federal government body that receives corporations' annual reports is the **SEC**
5. Which of the following are not included in an annual report?
    - **projections of the future stock price**
6. Net income is **profits remaining after income taxes are paid**
7. The current liabilities of a business may include **notes payable**
8. All of the following accounts are considered to be fixed assets on the balance sheet *except*: **depreciation**
9. What would be recorded in the *common stock par value account* on the balance sheet if 20,000 shares are issued at a par value of $2 and the market value is $5?
    - $20000 * 2 = 40000$
10. The financial statement that provides a snapshot view of the financial condition of a business at a point in time is the **balance sheet**
11. Financial and physical items owned by a business.
    - **Assets**
12. Creditors' claims on a firm, which are the financial obligations of the business.
    - **liabilities**
13. Cash and all other assets that are expected to be converted into cash within one year.
    - **current assets**
14. Devaluing a physical asset over the period of its expected life.
    - **Depreciation**
15. Shareholder wealth is measured as: **common stock price times number of shares outstanding**
16. The goal of a business should be **maximization of the owners' wealth**

17. SEC: **Securities and Exchange Commission**

Chapter 14

1. The method of evaluating the firm's performance over time is known as **trend analysis**.
2. Ratios used to compare different firms at the same point in time belong to a category of analysis called **cross-sectional analysis**.
3. Ratios used to compares a firm's ratios against average ratios for other companies in the firm's industry is called **industry comparative analysis**.
4. An analyst should be careful when conducting ratio analysis to ensure that **the overall performance of the firm is not judged on a single ratio**.
5. The primary purpose of the liquidity ratios is to determine **the ability of the firm to meet short-term obligations to creditors**.
6. Typically, assets and liabilities with maturities of one **year** or less are considered to be current for financial statement purposes.
7. Current assets / Current liabilities = **current ratio**
8. (Cash + Marketable securities + Accounts receivable) / Current liabilities = **quick ratio**
9. Net sales / Total assets = **total assets turnover ratio**
10. Net sales / Net fixed assets = **fixed assets turnover ratio**
11. Accounts receivable / (Net sales / 365) = **average collection period**
12. Total debt / Total assets = **total debt to total assets**
13. Total assets / Total equity = **equiy multiplier**
14. Earnings before interest & taxes / Interest expense = **interest coverage**
15. Net income / Common equity = **return on equity**
16. Earnings before interest & taxes / Net sales = **operating profit margin**
17. Net income / Net sales = **net profit margin**
18. The price/earnings ratio (P/E) is calculated as **stock price divided by earnings per share**.
19. A firm with total asset turnover lower than the industry average may have **insufficient sales**.
20. Earnings before interest and taxes (EBIT) is another way of describing **operating profits**.

Chapter 15

1. In general, the more net working capital a company has **the lower its risk**.
2. In general, the less net working capital a company has **the greater the risk**.
3. Calculation of a firm's average collection period is the same as calculating the **accounts receivable cycle**.

4. The time between when the firm pays its suppliers and when it collects money from its customers is known as the **cash conversion cycle**.
5. One type of investment that would not be suitable for marketable securities would be **mortgages**.
6. Assume net sales of $1,200,000 and cost of goods sold of $900,000. Determine the average investment in accounts receivable, inventories, and accounts payable. What would be the net financing need considering only these three accounts?
    1. Inventory period = Inventory/(COGS/365) –> $55 = \frac{I}{\frac{900000}{365}}$ –> $I = 135616.44$
    2. Receivables period = AR/(Sales/365) –> $35 = \frac{AR}{\frac{1200000}{365}}$ –> $AR = 115068.49$
    3. Payment period = AP/(COGS/365) –> $40 = \frac{AP}{\frac{900000}{365}}$ –> $AP = 98630.14$
    4. Net financing = AR + Inventory – AP –> $115068.49 + 135616.55 - 98630.14 = 152054.79$
7. A goal of a company's cash management policy is to **reduce the need to borrow**.
8. 5 C's of credit analysis
    1. Character – credit history
    2. Capacity – debt-to-income ratio
    3. Capital – money
    4. Collateral – assets
    5. Conditions – purpose of the loan